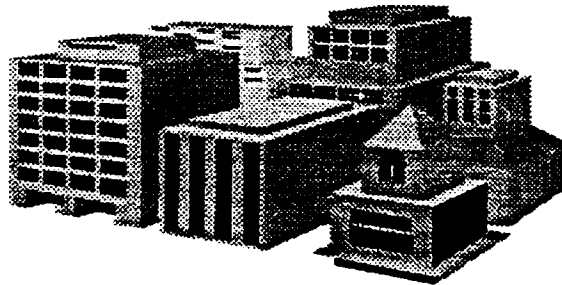


EUROPEAN UNIVERSITY INSTITUTE

DEPARTMENT OF LAW



RENT CONTROL LAW A COMPARATIVE STUDY OF DENMARK, GERMANY AND ITALY

A paper submitted

in candidacy for the LL.M. degree

by

FINN TRÄFF

Written under the supervision of

Professor Luis Díez-Picazo, E.U.I.

and

Professor Anna De Vita, Univ. of Florence

FLORENCE, ITALY

NOVEMBER, 1992

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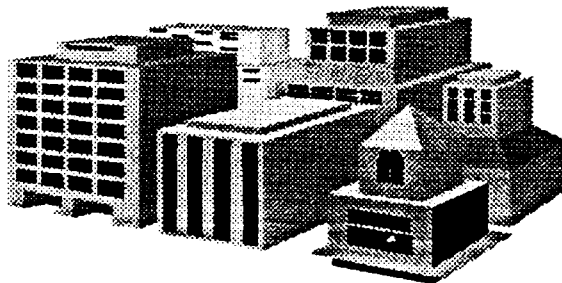
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LIST OF ABBREVIATIONS

BGB	<i>Bürgerliches Gesetzbuch vom 18. August 1896, (German Civil Code).</i>
boligreg.loven	<i>Lovbekendtgørelse nr. 525 af 11/8 1986 om midlertidig regulering af boligforholdene, (Danish Rent Restriction Act).</i>
BVerfGE	<i>Entscheidungen des Bundesverfassungsgerichts, (Decisions of the German Federal Constitutional Court). Official Reports.</i>
cod.civ.	<i>Codice civile, approvato con regio decreto 16 marzo 1942, n. 262, (Italian Civil Code).</i>
Corte cost.	<i>Corte costituzionale, (Decisions of the Italian Constitutional Court). Decisions are reported in Guirispudenza Costituzionale.</i>
legge n. 392/78	<i>Legge 27 luglio 1978, n. 392. -- Disciplina delle locazioni di immobili urbani, (Italian Fair Rents Act).</i>
lejeloven	<i>Lovbekendtgørelse nr. 524 af 11/8 1986 om leje, (Danish Rent Act).</i>
MHG	<i>Gesetz zur Regelung der Miethöhe vom 18. Dezember 1974, (German Rent Increase Act).</i>
UfR	<i>Ugeskrift for Retsvæsen, (Danish Law Reports).</i>

INTRODUCTION

Rent control is a policy of redistribution. When rents are controlled wealth is transferred from landlords to tenants.

Rent control law is not a new legal discipline; it has existed throughout most of this century in various countries. Today rent control exists in most European countries as well as in many countries outside Europe as well.

Somehow, it seems impossible for legislators to leave the important issue of housing completely to the free market, and it is noteworthy that many rent control regimes have been adopted recently.

When rent control is introduced the property rights of landlords are affected. Landlords cannot let their property at any price or at any condition they want; accordingly, they are restrained in their use of property. In turn tenants benefit from lower rents and security of tenure, which is a right to sit.

Property rights are acknowledged as extremely important in modern societies; they constitute a basis for capitalism and they can be seen as the basis for the economic order or society. In Denmark, Germany and Italy, property rights are protected constitutionally, and thus there are limits to the inroads that rent control can make on these property rights.¹ These limits can be seen both economically, as limits to the economic disorder that rent control can bring, and

¹See *infra* Ch. 3 n. 2.

as legal limits, i.e., limits to the inroads on property rights, as they are perceived legally.

Property rights cannot be described easily; ownership is not a single right that is clearly defined, but rather a number of rights. These rights can be obtained in different ways, and ownership itself can be described as many rights obtained a one of many ways.² Property rights can be seen as a multitude of rights, where words like *ownership* and *property* only become shells to cover these rights. Property rights are subject to regulation, and rent control law is only one of many regulations of private property rights, which can be found in a modern welfare state.

On the other side, the tenants' right to a home is important. The right to a place to live is a social objective, and if this right cannot be ensured through free markets, there is a need for regulation. It can be argued that the tenant's right to a home is a fundamental right in line with the property rights of the landlord, and that this right deserves a constitutional guarantee.³

This balance of interests between landlords and tenants creates problems for legislators and constitutional courts everywhere but it is much more a political issue, than a legal one. The legal basis for rent control is landlord and tenant law, a discipline within the law of contracts. Whereas the basic principles of landlord and tenant law show only small variations throughout Western Europe, rent control regimes vary greatly from country to country. These regimes seem to be established and changed with market fluctuations and they vary from

²See Ross (1951), pp. 468-484 and Ross (1953), pp. 206-211.

³This is the case in Spain and Portugal, though the right is not enforceable, see Ch. 1 n. 45.

something close to a free market with a slight element of consumer protection to complete controls based on tariffs.⁴

In many ways rent control law can be seen as a cross in the legal sphere. Landlord and tenant law is a classical discipline within the law of contracts. Rent control is a regulatory policy created by politicians to achieve economic and political objectives. Rent control has a huge economic impact on the distribution of wealth in society, and the legal problems of rent control may seem insignificant in comparison with the social and political effects of such legislation.

In turn, rent control law tend to be a very technical discipline, and legal studies tend to give emphasis to the details rather than to the concepts of rent control.⁵ However, in order to understand rent control, it is necessary to analyze the concepts and framework, rather than any specific legislation, which in many cases is drawn up with such a lack of coherence that a considerable discretion is left for those who apply the legislation.⁶

Rent control is often criticized, and economists in particular argue that it distorts free market operations. It is said that rent control leads to a housing shortage, immobility for tenants, homelessness for the poor, a screening of new tenants which leaves those who are expensive to serve without shelter, lack of

⁴Rent control regimes are often perceived as temporary, see *infra* Ch. 3 n. 54.

⁵Most legal literature tends to describe rent control law in detail, and only few studies try to conceptualize the principles of control, see Gärtner (1991), p. 477. As examples of more general literature, see De Vita (1985), and Paschke (1991).

⁶This is especially the case where normative expressions are used in legislation; e.g., in Great Britain and Ireland rents must be *fair*, see also Ch. 2 n. 1.

maintenance, a ceases of new building and black market operations.⁷ On the other hand, those who really benefit from rent control are not the poor, but the middle classes, who live in attractive neighborhoods where they are not obliged to pay a location premium, due to rent control.⁸

Although this criticism is put forward continuously, countries still apply rent control, and this leads to a first question: Why does rent control exist? Historically, rent control dates back to periods of shortage, and it was applied together with other rationing systems during the World Wars. However, in today's consumer society, where the free market prevails, it still exists. Why?

In order to answer this question, this will be a study of law *de lege ferenda*, which is a study aimed at describing law as it *should be* -- or a study of legal politics.⁹ When such a study is undertaken, the problem of bias which exists in all social sciences becomes obvious. Lawyers are not particularly skilled in politics, and it may be argued that a study *de lege ferenda* is not the business of any lawyer, because it involves setting up objectives for a policy. After all, in rent control, law is simply a tool which is used to achieve certain political objectives.¹⁰

However, according to Alf Ross, it is possible to make a study of legal policy, although with due respect to the objectives, which cannot claim any scientific truth, and accordingly the objectives of this research will be stated as clearly as

⁷For example, families with children.

⁸This criticism is described more in detail, *infra* p. 7.

⁹For the distinction between *de lege lata* and *de lege ferenda*, see Ross (1953), p. 385-416.

¹⁰See Ross (1953), p. 418.

possible in Chapter 1, where it will be discussed why rent control should be imposed.¹¹

The basis of this paper will be a comparative study between Denmark, Germany and Italy. In Chapter 2, the three legal systems will be described briefly, and some international considerations will be made. However, the main purpose of this Chapter is to provide information for further analyses.

In a study of legal politics the issue of constitutionality plays an important role. Constitutional provisions restrain legislators and constitutional review plays an important role in both Germany and Italy. In Chapter 3 the issue of constitutionality of rent control law will be examined in relation both to the landlords' property rights and to the tenants' right to a home.

Chapter 4 will be a structural analysis of rent control in the three countries. The study will be quite technical, and the task will be to find out how rent control works. The legal systems will be analyzed through three structural frameworks:

1. Contractual structures, which cover the contractual relationship, rights and duties of the parties.
2. Economic structures, which cover rents and rent increases.
3. Enforcement structures, which cover the enforcement of rent control and maintenance problems.

Through this analysis the legal systems will be described in more detail as they are compared, and this chapter will be the core of this paper

¹¹For a detailed description of how to carry out a study *de lege ferenda* see Ross (1953), pp. 417-431.

Chapter 5 will contain some points and conclusions.

Clearly, it is not possible in this paper to give a full account of rent control in the three countries which are compared. With emphasis on legal politics legal frameworks and statutes will be described. Only some very general provisions will be described together with some points of special interest.

It should be noted that rent control is only one policy among many housing policies, and it is sometimes closely interdependent on other policies. It is not the aim of this paper to describe housing policies in general, and accordingly there can be much more complex structures incorporating rent control than those which are described here.

Rent control applies to commercial tenancies in some countries, and in particular it should be noted that in all three countries the house market is divided into several submarkets.¹² Here only residential rent control will be treated. Social rental housing and subsidized rental housing are important for the provision of housing, and rent control of some kind applies to these sectors which have been set up to provide affordable housing.¹³ Private non-subsidized rental housing is the area in which the contradiction between the objectives of a social policy on the one side, and the property rights of landlords on the other become clear, and this sub-market will be the subject of this paper.

¹²This is the case in Denmark. A special act, Lov af 21/12 1988 om lejeregulering i erhvervslokaler mv., applies to commercial tenants.

¹³For example, in Germany subsidized rental housing is controlled through a special legal framework, see p. 32.

CHAPTER 1

OBJECTIVES OF RESEARCH

In the law of contracts the parties are free to set up their agreement, and when they have done so, they are bound by their agreement. In this way the parties have an autonomy, which does not only include a freedom to act, but also a freedom to give up this freedom by binding themselves to a contract. This autonomy of the parties can be seen as the legal counterpart to the free market in a capitalist society. The freedom of the individual to make his own choice, to maximize his profits through bargaining and to enter into any contract he wants. This is essential for free market operations, and accordingly, it is the most important task of the law of contracts to ensure that this autonomy of the parties is guaranteed.

However, apart from this very basic principle of autonomy, there are two main branches of law within the law of contracts, variable and invariable law. The distinction between the two branches is independent of legal disciplines, and the distinction can be seen in the objectives for legislation.

Variable law is meant to fill in the contract of the parties. Many contracts are established in a very simple manner, and the parties have not foreseen all eventualities.¹ Variable law provides standardized solutions to disputes. The parties are free to agree on other solutions than the ones provided by variable

¹For example, when a purchase is made in a shop, the parties rarely sign a written contract, where it is agreed, how to treat defects.

law, and in a conflict between the content of the parties' agreement and variable law, the agreement prevails.

Invariable law, on the other hand, is meant to give certain guarantees to the parties. It is applied in order to avoid that the weaker party is exploited by contractual conditions which are burdensome.² Invariable law limits the autonomy of the parties, and it is therefore not in accordance with the basic principle of law of contracts. In turn, the objectives for invariable law must be found elsewhere, in consumer protection issues, social rights, etc.

Landlord and tenant law is a discipline within the law of contracts like law of purchase, insurance law, etc. Something of value is given in return for a performance or a promise of performance by the other party. In the case of landlord and tenant law, the performance of the landlord is to give the tenant possession of property, and the performance of the tenant is to pay a rent. Also in landlord and tenant law, the legal basis is the autonomy of the parties. They have opposed interests, as the landlord wants to obtain as high a rent as possible, while the tenant will be interested in paying as little as possible. As a starting point, the parties should be able to find the right balance between interests through bargaining. However, the parties are uneven from the very beginning; landlords have primarily an economic interest in the contract, while tenants have an interest, which also has a social dimension.³ Moreover, leases are very complex contracts, and there are many questions apart from the size of the rent that the parties need to agree on. These obligations are not characteristic for the contract and therefore they are called by-obligations. They can

²For example, a provision which allows tenant's to sublet their property can be made invariable, and accordingly the parties cannot agree on a clause according to which the tenant's cannot sublet. See in Danish law, lejeloven §§ 69-70 and 79.

³See Radin (1986), pp. 359-368, De Vita (1985), p. 349 and Derleder (1987), pp. 39-41.

be the size of deposit, maintenance obligations and other duties of the tenant or the landlord.⁴ For these reasons, it has been necessary to leave the principle of freedom of contract, and to introduce some protective legislation, rent control law.

In rent control law, the key issue is the limitations to the parties' freedom of contract. Whereas the autonomy of the parties is a starting point, inroads are made into this autonomy through the use of invariable law. Such inroads are made not only through lower rents, but also through invariable clauses concerning by-obligations, as such obligations can have a very important impact on the outcome of the entire contractual relationship between landlord and tenant.

These other conditions -- by-obligations become particularly interesting for the landlord under rent control, because a change of by-obligations can be one way of compensating for lower rents. In this way, the landlord may try to increase his income from the property or to lower his costs.⁵ For the tenants,

⁴For example, when parties enter into a contractual relationship, the relationship is distinguished by its most important features, i.e., purchase is distinguished as an exchange of goods for money, insurance is distinguished as an exchange of guarantee for money, rent is distinguished as an exchange of the right of using something for money. These features are the main obligations that characterize the contractual relationship, and thus obviously the most important. If one of the parties fails to fulfill his main obligations the other party will be able to state a breach of contract. There are, however, also by-obligations. They are obligations, derived from the same contractual relationship, but they are not characteristics of the contract, i.e., the landlord's obligation to maintain the house is a by-obligation. Another example can be the tenants' obligation to keep the garden in good order and to keep quiet at night.

⁵For example, if tenants are obliged to carry out maintenance work on the property, this corresponds to an additional rent paid by the tenants. Also if tenants are not allowed to keep a dog in an apartment, other apartments in the house will benefit from less noise and dirt, and the wear of the house will be less, though extremely marginally.

by-obligations often do not seem very interesting, when the contract is signed. There are so many clauses in a lease, that it becomes virtually impossible for the unskilled tenant to go through them. Moreover, by-obligations are normally presented to the tenant on a printed contract form, which can be taken -- or left. Any negotiation before entering into a contract will tend to concentrate on a few key issues such as the rent and other issues of immediate significance, such as deposit and period of contract.

The length of contract is a particular issue of interest to both parties, and this matter is subject to invariable provisions in both Denmark, Germany and Italy. The landlord will generally benefit from a short-term contract, as it will be possible to renegotiate the contract (and to increase the rent) at the end of each term. Moreover, a short-term contract makes it easier for the landlord to change the use of the property.⁶

At the same time, the tenant will be interested in a long term contract, which will guarantee his right to stay in the property, i.e., security of tenure. This right is extremely important for the tenant, it is a social issue, a right to maintain a home. The tenant will be weak in bargaining with the landlord and reluctant to enforce rent control if the landlord can use eviction as a retaliatory measure. A contract, which provide security of tenure will protect the tenant against such measures.

Security of tenure implies not only a right to stay, but a right to stay under the same conditions as originally accepted when the contract was entered into. If the contract can be changed (and the rent is raised), the tenant is required to

⁶For example, if the property is required for occupation by the landlord for himself or his relatives, or if the landlord wants to use the property for purposes other than rental housing. See Stanbury and Todd (1990), p. 403-406.

pay more for the same property, and even though increases may only compensate for inflation, there is no guarantee that the earnings of the tenant have gone up correspondingly. Consequently, any change in the conditions of contract must be seen as interference in the security of tenure, as the changes may go beyond the tenant's economic abilities.⁷

However, tenancies are often long lasting or even lasting for an indefinite time. After some years it can happen that a difference occurs between the original rent and the actual market rent. In this situation the landlord has a vested interest in a rent increase.⁸

In the law of contracts, a lasting contract can be modified unilaterally with the same notice as is required for termination. This can be constructed legally as a termination combined with an offer for renewal, for example, if a bank raises the interest rate, or an insurance company raises the premiums, their clients are free to change.⁹ If the tenant has been granted security of tenure through invariable provisions, the landlord cannot terminate the contract, and demand a rent increase. So, if there are going to be any rent increases at all, there must be a legal framework according to which rent increases are allowed.

Rent control regimes offer a solution to this problem, as rent increases are controlled. However, the tensions of long lasting tenancies cannot be freed

⁷The security of tenure is recognized as a very important matter by many writers. Tenants live in their property, and their homes have an important social function, which must be acknowledged. See, e.g., Radin (1986), pp. 359-368, Paschke (1991), pp. 75-94, De Vita (1990), pp. 40-46, Stone (1986), pp. 627-656.

⁸If landlords are not allowed to charge market rents, the value of their houses will fall correspondingly, and tenants rather than landlords will benefit from capital gains, which are a result of the investment in houses.

⁹This is elementary (variable) law of contracts. See, e.g., Gomard (1986), pp. 24-25, Brox (1983a), pp. 113-114, Brox (1983b), pp. 106-107, Krag Jespersen (1989), p. 17.

without endangering the security of tenure, and the balance between a tenant's right to security of tenure on one side, and the landlord's right to a return on his investment seems to be one of the most delicate balances in rent control legislation.¹⁰

There is also a strong element of consumer protection in rent control, because the tenant is protected from entering into a contract which may later cause hardship. In particular in relation to some of the by-obligations the issue of consumer protection seems to be important, as the value of such clauses is not high, and the tenant does not realize their importance until it is too late.¹¹

Accordingly, some contractual protection of tenants is needed even in a society without rent control -- from a consumer protection point of view, and the use of invariable law in landlord and tenant relationships is in line with current trends

¹⁰A parallel can be drawn between rent control and monopoly price control, as the landlord is in reality in a monopolist position when a rent increase is proposed. The tenant, who has a strong wish to stay, is in reality forced to pay any price asked by the landlord, and rent control is a way to prevent exploitation of tenants.

¹¹Consumer protection appears in all kinds of contracts where one party is a professional and the other party a consumer. First, there is a need to protect the relatively weak consumers against conditions set up in contracts which will deprive them of their expectations -- or what is said to be a minimum protection. For example, a consumer expects to be able to return a defective production. In these situations legislators often use invariable clauses, which cannot be changed through an agreement between the parties. See Paschke (1991), pp. 455-459. Second, there is a need to inform consumers of their actual obligations and rights, such as how much they actually have to pay back on a loan, interest rates on credit cards, and their right to cancel orders, see *infra* p. 78. Third, standard contracts are interpreted in favor the one who did not set up the contract, i.e., the consumer.

These arguments in favor of consumer protection cannot be ignored. Even in a community without rent control, it is necessary to have some kind of consumer protection. A central issue becomes how far to extend the consumer protection to give tenants security against unreasonable and unexpected clauses, and at the same time not to interfere with the right to set up a contract freely.

in favor of consumer protection, which can also be seen in other legal disciplines, for example, insurance and labor law.¹²

Under rent control the problem becomes more serious. Rent control regimes intend to establish rents lower than the market level. Accordingly, the parties should not be able to compensate for lower rents through burdensome contracts. At the same time the tenant has very little bargaining power under rent control, as he cannot leave the contract to go somewhere else. Consequently, rent control cannot be effective unless the contracts are also controlled. The level of rents cannot simply be isolated from other conditions linked to the contract.

In this way rent control can be seen as a way of using invariable law to protect the relatively weak tenants in a situation where the autonomy of the parties would be unable to provide a well-balanced outcome of negotiations between the parties.

The economist's approach

Much criticism of rent control is based on economics, and it is necessary to go through some very basic economics in order to give an account of this criticism.

In an open and free market, prices are set by supply and demand. There are a number of suppliers, who compete on prices. If demand rises, prices will rise too and more suppliers will find the market attractive. On the other hand, if demand falls, suppliers will lower prices, and eventually some of them will leave the market. At the same time a change in prices influences demand, as more or

¹²Some authors will point out that landlord and tenant law and labor law in particular are special disciplines within the law of contracts, and that traditional concepts of autonomy do not apply to these disciplines. See Paschke (1991), p. 21. De Vita (1985), p. 349 goes further and sees the right to a home as a fundamental right.

fewer people will find the commodity affordable. As a result, this mechanism works towards a new balance, an equilibrium, where prices ensure that supply meets demand.¹³

It can be said that the market mechanism ensures that goods are available for those who are willing to pay the most, while people with less will or ability to pay will not get the same goods or the same quality of goods. In a free market, prices function as a discriminator, a device for allocation of goods. They ensure that goods are allocated according to the preferences of consumers. In the case of housing this means that rent will be set according to the desirability of the property. If the rent is set too high, tenants will go elsewhere. If the rent is set too low, tenants will queue for the property, and thus allow the landlord to raise the rent.¹⁴

When rent control is introduced, an artificial maximum for rents is created. This influences supply and demand in the housing market.¹⁵ The supply will fall, as landlords try to find an alternative use for their property, and it will also prevent entrepreneurs from undertaking new construction, as rent control reduces the expected return on new investments.¹⁶

¹³See Lipsey et al. (1987), pp. 101-107 and Robinson (1979), pp. 75-76.

¹⁴See Nessler (1988), p. 98.

¹⁵This maximum rent under rent control must be lower than the market rent, otherwise the rent control is not efficient, see Boligmarkedet og boligpolitikken -- et debatoplæg (1988), p. 86.

¹⁶For example, by converting property into condominiums, which can be sold at free market prices, by letting the property as non-controlled office space or even by opting out of the market and leaving the property unused. See Stanbury and Todd (1990), pp. 403-406 and *infra* p. 132. For a more general approach to rent control and housing economics, see Albon and Stafford (1988), pp. 10-21, Welfeld (1988), pp. 110-120, Nessler (1988), pp. 96-100, Moorhouse (1987), pp. 6-24, Robinson (1979), pp. 75-97. See also Ivatts (1988), pp. 206-208, who argues a removal of rent control will not end the current disinvestment in private rental housing and Kemp (1990), pp. 145-155, who replies.

Meanwhile, demand will increase. More people will be able to afford more and better housing as prices are lower.¹⁷

The combination of the two, lower supply and higher demand creates a housing shortage. There will be more people willing to rent property than there is property available, and hence there is no equilibrium in the price of property. It can also be said that prices are not allowed to function as discriminators.

In turn, this leads to a new balance point, an equilibrium in contracts.¹⁸ The right to obtain a property at a controlled price will have a value, and key money will make up for the difference between the controlled rent and the market rent. However, key money is often forbidden under rent control; and without economic measures for the allocation of vacant property, other non-economic mechanisms will come into force.¹⁹

These mechanisms include queuing for vacant property, random selection of new tenants, screening procedures and nepotism.

Screening procedures can help the landlord to keep down costs by choosing tenants who are not likely to cause trouble, or tenants who will minimize maintenance costs, for example, single person households, households without children or pet animals, etc. However, screening can also be used to dis-

¹⁷It can be argued that everybody needs housing anyway, and thus the consumption of housing goods is stable, and that it is only the supply that is in question. In fact, the consumption of housing can change greatly, depending on the standard of housing, on the number of rooms occupied by each individual, etc. See Boligmasse og boligkvalitet, Boligministeriet 1990, p. 110, where it is argued, that even though the Danish housing market is near saturation point, calculated as a dwelling for every family or single person over 20 years of age, it still cannot be said whether demand will continue to increase.

¹⁸See Weber and Wiesmeth (1987), p. 60.

¹⁹See *infra* p. 103 about key money.

criminate against ethnic or religious groups, or for other reasons, as the landlord is free to choose his tenants.²⁰

Nepotism sounds negative, but is in fact a perfectly legitimate and understandable mechanism in the private housing market. Landlords who are forced to let property at controlled rents might justifiably favor friends and relatives, rather than take unknown tenants. However, nepotism helps to maintain a pattern in which those who really benefit from rent control are those who can obtain controlled property through friends, relatives, etc. In other words economic discrimination has been substituted by discrimination based on social networking abilities, and there is absolutely no guarantee that such discrimination favors poor people.

Landlords will also try to lower costs. This can be done by lowering the standard of maintenance of a property. The value of the dwelling decreases as the maintenance standard goes down, but the economic return to the landlord remains the same. The landlord does not risk tenants moving out or demanding lower rents until the standard reaches a point at which the market value of the property falls below the controlled rent. Furthermore, investment in new houses becomes unattractive, and the housing stock as a whole decreases.²¹

It is claimed that this process of deterioration in turn leads to homelessness as the lack of new construction under rent control leads to a smaller supply of

²⁰Obviously, screening can also occur in non-restricted markets. However, under rent control screening has no economic consequences for the landlord, as he does not need to accept lower rents by excluding some prospective tenants. See Miron (1990), p. 168 and Loikkanen (1985), p. 500-503.

²¹See Stanbury and Todd (1990), p. 404, Albon and Stafford (1990), p233, Albon and Stafford (1988), p. 15-16, Baar (1983), p. 830.

housing.²² Maintenance cannot simply be seen narrowly, as single buildings allowed to deteriorate, but also in a broader sense, as landlords have no incentive to maintain a sound housing stock.

In short, these economic arguments can be presented as two main arguments. First, the allocation argument -- rent control creates a shortage of housing, and other discriminators start working. Second, the maintenance argument -- rent control does not allow proper maintenance of the housing stock.

From an economist's point of view the only way to solve these problems is to return to a free market, where rents are set according to supply and demand. If rents are too high from a political point of view, the housing stock must be increased to obtain a new equilibrium with lower prices.

The allocation problem will exist for as long as there is a housing shortage, and as the shortage is created by rent control, there will be a problem, for as long as there is rent control, i.e., for as long as a segment of the house market is considered to be so relatively *cheap* that people will compete to obtain the vacant dwellings there rather than move on to other sub-markets.

Rent control may be able to absorb some price shocks in a volatile market, but if rent control becomes a permanent measure the market will not provide capital for maintenance and construction of new dwellings, and the standard of housing available will eventually become lower. To put it very simply, one cannot expect the market to provide funds for maintenance of the housing

²²The argument of rent control leading to homelessness must be seen together with filtering, which is a process where housing services, become available for low-income tenants, when high-income tenants move out, see Weicher and Thibodeau (1988), pp. 21-24. It can be argued that this process is halted by rent control. For a view on this argument, see Tucker (1990), Quigley (1990), p. 89-93 and Appelbaum and Gilderbloom (1990), pp. 605-606. See also Welfeld (1988), p. 120.

stock when it is not allowed to work. As a consequence new construction must be financed with public funds.²³

The Ølgaard committee's reports

In 1988 and in 1990, the so-called Ølgaard-committee was appointed by the Minister of Housing in Denmark. The task of the committee was to carry out a survey of the use of the housing stock and the economic conditions in different sub-markets. Against this background the committee should put forward suggestions to loosen the tensions in the housing market, and to deal with the allocation problems and the maintenance problems identified. The committee has so far submitted two papers: "House Market and House Policy -- a discussion paper" and "House Stock and House Quality -- a discussion paper".²⁴

One of the most important conclusions so far is that the housing market in Denmark is near saturation point. At present there are sufficient dwellings for every couple and every single person over the age of 25 years. Within 10 years the number of dwellings will have increased, so there will be dwellings for every couple and every single person over the age of 20 years.²⁵ As the Danish housing market is divided into smaller submarkets this tendency will appear first in the most expensive market, the market for home ownership. At the same time, there will still be a housing shortage in the cheapest market, the rent controlled market for private tenancies.

²³Albon and Stafford (1988), p. 20, Nesslein (1988), p. 104-106. Boligmasse og boligkvalitet (1990), p 120-122.

²⁴Boligmarkedet og boligpolitikken (1988) and Boligmasse og boligkvalitet (1990).

²⁵Boligmarkedet og boligpolitikken (1988), p. 60.

In the market for private ownership some of these tendencies have already been seen, as this market has experienced falling prices twice during the eighties, and it is no longer likely that the situation will return to that of the sixties, where there were consistent capital gains in this market. This is the only non-controlled sub-market, although heavily subsidized through tax relieves on interest paid on mortgages. The committee fears that further subsidies to privately owned housing, combined with saturation of the house market, will lead to problems for social tenant housing, in which houses are generally newer and more expensive to live in than private rented houses.²⁶

Subsidies and rent restrictions cause an increased demand for housing, which in turn creates a housing shortage, because more people can afford to have their own property at a young age, and some people want to have more property. The social costs of a given house consumption are unclear, and the necessary urban renewal is achieved only through subsidized urban renewal programs, where neither the landlords nor the tenants pay the real costs of the renewal. In turn the renewal becomes disproportionately expensive, as nobody takes an interest in cutting costs.

As much of the housing stock is about 100 years old and needs renewal, the current policy leads to considerable public expenditure, and the committee believes that the benefactors, i.e., the tenants and the landlords, should pay a larger part of the renewal costs. For the tenants this will inevitably lead to higher rents.

The Committee estimates that an annual cost of approximately DKK 80-100 per square meter is needed for the upkeep of buildings on average. According to

²⁶Boligmasse og boligkvalitet (1990), p. 111.

the Rent Restriction Act, landlords are only allowed to allocate DKK 56 annually for this purpose when they calculate the rent.²⁷

Another problem is the so-called *rent span*, which is a difference between rents within the housing market that cannot be explained by differences in the quality of houses. The rent span occurs especially among dwellings of different ages, as rents for old houses are calculated at a lower level than rents for new houses. The rent span is due only to restrictions, and the consequence of a rent span is that rents are to a certain extent set without relation to the actual value of the dwelling. In a controlled market this means that the worst property is relatively more expensive than the best, as calculations are based on units, square meters, etc., rather than location and other very desirable qualities, which are ambiguous.

The rent span leads to an allocation problem as there will be queuing for the most attractive property in a controlled market, even when there are vacancies in less attractive, i.e., more expensive sub markets, and it is concluded that the housing shortage in Denmark cannot be solved through new construction, as people queue for cheap and good property only.²⁸

The main suggestion of the committee is to increase rents across the board. In this way more money can be allocated to the maintenance of houses. However, politically the conclusions of the committee have not been very well accepted in Denmark.

The committee also suggests a deregulation of the housing market, and at present only a few steps towards deregulation have been taken, most note-

²⁷Boligmasse og boligkvalitet (1990), pp. 116-122. The Committee suggests a rent increase, and in turn suggests that capital gains deriving from the rent increase should be taxed.

²⁸Boligmarkedet og boligpolitikken (1988), p. 134.

worthy being that rents for most new private construction after 1/1 1992 are free from control.²⁹ This may not be of great importance, however, as cost controlled rents for new construction were at a level well above that which the market was able to bear.³⁰

The committee, which is composed of economists, concludes that the Danish housing market is subject to plan economy -- without a well-defined plan,³¹ and their conclusions seem to be very much in line with the general criticism of rent control made by economists elsewhere,³² as emphasis is given to market distortion and the need for public funding. On the other hand in this criticism little consideration has been given to security of tenure and consumer protection, as the tenants' ability to pay the rent is regarded as an issue of social policy, rather than of housing policy.³³

Objectives for further research

There are three arguments which in general are put forward in favor of rent control; and in order to set up objectives for this report, it is necessary to examine these arguments.³⁴

1. Windfall profits, or excessive profits.
2. Affordability.
3. Security of tenure.

²⁹Passed by the Danish Parliament as Lovforslag nr. L63, vedtaget d. 19/12 1991.

³⁰Boligmarkedet og boligpolitikken (1988), p. 19.

³¹Boligmarkedet og boligpolitikken (1988), p. 164.

³²For example, Albon and Stafford (1987).

³³Boligmasse og boligkvalitet (1990), p. 110.

³⁴These three arguments have been described by Hanly (1991), pp. 191-197.

Profits are generally perceived as acceptable in a capitalistic society, and windfall profits do not seem a problem in themselves. Only if windfall profits lead to hardship for others, either by creating affordability problems or by endangering the security of tenure, do they become unacceptable.

Moreover, windfall profits is a normative term, as the term implies profits which are higher than they *should be*. To define windfall profits, it is thus necessary to find out how big profits *should be*. This makes windfall profits extremely difficult to handle, because it is an impossible task to set a standard for how big profits *should be*.

If a market functions efficiently, there should be no such thing as windfall profits, as supply and demand will meet at what is supposed to be the right price.³⁵

It can be argued that if the only problem is high profits, it would be more useful to react against them through taxation than through regulation.³⁶ Taxation does not distort the market, and at the same time it brings money into treasuries.

It is also noteworthy that many American cities have introduced rent control during the last 20 years.³⁷ Rent control has thus become an extremely popular political measure in big cities, and this development cannot be explained simply by a strong wish to cut profits.

Consequently, windfall profits cannot be seen alone, but rather as an additional normative argument used when a real problem occurs, i.e., a problem of affordability or security of tenure.

³⁵For a discussion of the efficiency of the market functions in the case of housing, see Nesslein (1988), pp. 95-106.

³⁶Boligmarkedet og boligpolitikken (1988), p. 117.

³⁷See Appelbaum and Gilderbloom (1990), p. 601 and Baar (1983), note 1.

Affordability is a relative term; what may be unaffordable to some may be affordable to others and the problem of affordability is, as pointed out by the Ølgaard-committee, a problem of social policy rather than housing policy.³⁸

An attempt to solve an affordability problem through rent control will immediately run into other problems. Controlled property is not necessarily rented to poor people, and rent control favors everybody who lives in controlled property, regardless of their income. Moreover, as it has been pointed out, rent control leads to an artificial housing shortage, which in turn creates an allocation problem where alternative allocation mechanisms start to work, and there is no guarantee that these mechanisms work in favor of poor people. As a result the use of rent control to provide affordable housing may turn out to be a social policy in favor of the wrong people.³⁹

Moreover, a far more adequate remedy for affordability is rent allowances, which are given to tenants on the basis of their income and household. This system is used together with rent control in both Denmark and Germany.⁴⁰

As a result, rent control seems to be an inadequate measure to provide affordable housing as housing markets work in the same way as other markets based on supply and demand, and any attempt to bring rents below the equilibrium will run into economic problems such as the allocation and maintenance problems described.

Apart from the economic arguments against rent control, the tenant's right to stay in his property has also been pointed out above. Security of tenure is a

³⁸See Boligmasse og boligkvalitet (1990), p. 110 and Goyorko (1990), p. 791.

³⁹See Welfeld (1988), pp. 113-115, Albon and Stafford (1988), pp. 16-17.

⁴⁰See for Denmark, Lovbekendtgørelse nr. 467 af 1/8 1988 om individuel boligstøtte; for Germany, Wohngeldgesetz in der Fassung der Bekanntmachung vom 28. Februar 1990.

very important social right; for residential tenants it is the matter of the right to a place to live.

If a residential tenant, for one reason or another, is forced to leave his home, it is not only a matter of inconvenience and moving costs. At the same time the tenant is forced to give up the center of his activities. The neighborhood, the children's' school and the social network are very important factors in the life of the individual. Security of tenure can thus be seen as a fundamental right.⁴¹

The direct effect of this need for protection of tenants is protection against eviction. In Denmark and Germany, landlords cannot evict tenants for any reason or at their discretion. Only when the eviction is *justified* can it be allowed.⁴² Other countries, such as France and Italy, have systems where security of tenure is guaranteed by contracts of a certain minimum period.⁴³

Moreover, in Denmark or Germany security of tenure is regarded as a part of the permanent law of contracts, as the relevant clauses are now placed in the main acts.⁴⁴ In both countries, acts were amended during the seventies, and it

⁴¹See *supra* n. 7.

⁴²See *infra* Ch. 3 n. 34.

⁴³ In Italy this period is 4 years. See *infra* p. 38. In this way legislators have tried to balance the landlord's right to take back his property with security of tenure. It can be seen as an attempt to pursue the ideal solution when it comes to balancing rights. However, the success of such a solution is certainly arguable, and additional guarantees are often given to special groups of tenants, or security of tenure is otherwise enhanced, see *infra* p. 37. In general such additional guarantees can be given in several ways; either by hardship clauses, which allow individual tenants to stay, if they will otherwise suffer hardship, see *infra* p. 97, or by a general ban on evictions, which is known in Italy. In any case, the result is a tendency towards a complete security of tenure.

⁴⁴See *lejeloven* §§ 82-83 and *BGB* § 564b.

can be seen as a move towards a political recognition of the security of tenure as a fundamental right, a right that tenants cannot be left without.⁴⁵

Security of tenure is closely linked to the size of the rent, as it has already been pointed out; and as a starting point *any* rent increase endangers a tenant's position. A rent increase is fundamentally a change in the original contract, and it can -- depending on the size of rent increase and the tenant's ability to pay -- force the tenant to give up his property. In the political process leading to rent control this is a very important question. Some of the first rent control regimes were imposed as war-time rationing during the First and Second World Wars, and they consisted of a general ban on evictions combined with a rent freeze, which was obviously protection of the sitting tenants. Consequently, there is a connection between the two which goes both ways, as rent control is necessary to ensure security of tenure and vice versa, and it is debatable which one of them leads to the other.⁴⁶

⁴⁵Even though the right to a place to live can be seen as a fundamental right, it is rarely found in constitutions, and -- like other social principles -- it could rarely be enforced. Examples of a constitutional right to a home can be found in the Spanish Constitution, art. 47 and the Portuguese Constitution, art. 65. According to the Spanish Constitution authorities are obliged to promote decent housing for all Spaniards. However, the article is not directly enforceable according to art. 53 of the Constitution. Also the Portuguese constitutional provision is not directly enforceable.

⁴⁶There is a recent example of the political importance of security of tenure in Denmark. Commercial tenants were decontrolled in 1975 with an act which allowed rent increases every second year. Rents could be raised to the level of comparative rents in the neighborhood. In about 1985, there was a boom of rents in central Copenhagen, and many commercial tenants were met with very steep rent increases. Many shops, which were well situated and which had benefited from low rents for many years, were forced to move. This led to the founding of a commercial tenants' association and lobbying for economic security of tenure for commercial tenants. (Contractual security of tenure existed already, as commercial tenants are covered by the Rent Act).

However, it seems that it is security of tenure that leads to rent control and not the other way around. It has been argued that security of tenure is the key issue of rent control, i.e., to protect the tenants right to stay in their property, and to maintain their homes for as long as they wish, without suffering any hardship for this reason.

The windfall profit argument is a false argument, based on vague ideas about how big profits should be, and affordability problems can be solved more adequately through social policy. As a result of this first conclusion security of tenure will be the key phrase in this report.

However, the question of affordability cannot be completely discarded, as rent control may be an inadequate solution to the problem of the provision of affordable housing, but it still remains to be explained why rent control is so popular among politicians. With rent control in more than 200 jurisdictions in the United States, most European countries and many other countries around the world, it is an important question to ask.⁴⁷

Rent control contains an element of spreading welfare, i.e., an element of taking from the rich and giving to the poor. Even though economists argue that it does not solve any problems in the long run, as it simply -- over a time -- reduces our housing consumption through lack of new construction and maintenance, a rent control policy may still seem to be a cheap way of

This lobbying led first to a temporary freeze of commercial rents, second to the Commercial Rent Act (Lov af 21/12 1988 om lejeregulering i erhvervslokaler mv.), which restrained landlords' possibilities for increasing rents. The principle of rent increases remains the same, but the Act has some built-in delay factors, which means that a rent increase cannot be argued on the basis of comparable tenancy agreements closed within the last year, and that rent increases may only coming into force gradually over a 4 year period.

⁴⁷See *supra* n. 37.

providing affordable housing. It is cheap, because there are no or few public expenses as a direct consequence of rent control.

The question arises of how much we should spend from our income to live in decent surroundings, and what are decent surroundings. These questions may very well be asked within the scope of this subject, as a rather awkward problem occurs if housing consumption becomes "unacceptably expensive" from a social point of view. However, this very interesting question goes far beyond the scope of this paper.

Some issues of consumer protection evolve during the discussion of rent control, as matters cannot be separated. The sheer volume of clauses in a contract calls for consumer protection. However, consumer protection itself is not a product of rent control legislation, and nor does consumer protection lead to rent control. The main problems of consumer protection are to ensure that tenants get a reasonable, predictable and comprehensive contract.⁴⁸

Many of the problems mentioned above which are caused by rent control are results of price regulation, rather than direct consequences of security of tenure, and there is no reason for rent control to be more restrictive than necessary to secure the tenure.

Security of tenure will be considered as the objective for rent control legislation. Affordability and consumer protection will not be treated as issues of special importance in this report, though these objectives will be mentioned, and in other contexts they may prove to be extremely important.

⁴⁸Consumer protection can be seen as a matter of standardization of commodities, whereas rent control is a matter of price regulation. However, especially in contractual rent control, *infra* p. 76, the two are difficult to distinguish from each other, and some arguments of consumer protection will be brought into consideration.

Rent control is basically an interference in the free market formation and rent control law is invariable provisions which modify the basic principle of autonomy of the parties. Rent control creates distortions, and these distortions are pointed out as drawbacks, the objective of this paper will be to examine to what extent it is possible to reinstate free price formation with emphasis only on the key issue, that which is really important for tenants, security of tenure.

In other words: how can security of tenure be provided with as little impact as possible on the landlords' economic use of their houses? Or even simpler: how much or how little use of invariable provisions in legislation is needed to give tenants security of tenure?

CHAPTER 2

A COMPARATIVE APPROACH

In a comparative approach to law, it is important to analyze legal systems which show differences. In this way the legal systems compared can each contribute in a different way to the understanding of rent control. The choice of Denmark, Germany and Italy for comparison has been a choice of chance. However, there were certain reasons *not* to choose some other legal systems that can be pointed out.

In the United States and Canada, rent control is implemented on state or city level, while in Europe legislation is made country by country. This does not prohibit comparison, but it certainly makes comparison more difficult, because rent control legislation and the protection of tenants contractual rights may be found on different levels of legislation. Moreover, these countries are not European. This is no disqualification, but as there may be a harmonization among the EEC countries also in this field of legislation, it might be more interesting to limit the study to countries within the EEC.

British and Irish legislation are based on a legal tradition fundamentally different from that of continental Europe. In a study of legal frameworks where the objective is clearly defined *de lege ferenda*, these systems are extremely difficult to compare with the systems of continental Europe. This is not because

the legal systems are that different, but the description of law in Britain and Ireland is more cumbersome than that used in continental Europe.¹

The choice of Denmark, Germany in Italy covers some important trends in housing policy, and at the same time the countries are not that different when it comes to the general law of contracts. Germany and Italy have a structure with civil codes, which contain the general landlord and tenant law, and special acts concerning rent control. The same pattern is followed in Denmark, where, however, there is no civil code, but a number of general acts that cover approximately the same legal fields. Among these acts there is an act concerning rent of real property.

¹The British and Irish legal acts seem incomprehensible to me. The acts are often very long, and they contain many definitions and repetitions, e.g., in the Irish Housing (Private Rented Dwellings) Act, 1982 tenant is defined in section 7 (1): "'tenant" means the person for the time being entitled to the possession of a dwelling to which section 8 (1) relates and includes a person - (a) who would, at the commencement of this Act, be the tenant of the dwelling if the Rent Restrictions Act, 1960, and the Rent Restrictions (Amendment) Act, 1967, had full force and effect at times from their passing until such commencement, and (b) who is in possession of the dwelling at such commencement, and (c) whose tenancy is not a tenancy in respect of which an order for possession has been made under section 5 of the Rent Restrictions (Temporary Provisions) Act, 1981." Such a definition seems superfluous, and moreover when it comes to the key issue, the actual rent control in Irish law, section 13 (2) of the same act states: "For the purposes of subsection (1), the gross rent shall be the rent which, in the opinion of the Court, would be a just and proper rent having regard to the nature, character and location of the dwelling, the other terms of the tenancy, the means of the landlord and the tenant, the date of purchase of the dwelling by the landlord and the amount paid by him therefor, the length of the tenant's occupancy of the dwelling and the number and ages of the tenant's family residing in the dwelling." On this basis, it is completely up to the rent officers and the Court to decide even the main principles for rent control, and in the legal literature, it can be argued which principles are used, see, e.g., Madge (85), pp. 833-35 and 851-852. The British and Irish legal systems may work perfectly well, but from a continental point of view they do not seem good examples.

Though Denmark, Germany and Italy will cover some of the most important trends in rent control today, it is worth noting some policy trends in other countries, which will not be compared here. In Sweden there is a unique system of collective bargaining.² In Britain rents were deregulated in 1988.³ In

²Sweden has a long tradition of collective bargaining in the field of rent control. Landlord and tenants' organizations bargain over the size of rent increases and over contractual conditions, and the result of this bargaining is applied to the contracts between the individual landlords and tenants.

In the case of a dispute, the parties are obliged to bargain before the case can be taken to tribunal. Yet, when a case is taken to the tribunal, the rent is decided on the basis of a comparison with rents for equivalent dwellings. Thus, the bargaining process is conducted within the guidelines of the expected decision of the rent tribunal, and the costs of litigation, which are paid by the parties themselves, work in favor of an agreement. Individual tenants can also contest the outcome of the collective bargaining process, and consequently it seems that the bargaining process has more to do with the procedural approach to rent increases than the actual level of rents.

Rents are decided on the basis of rents for comparable property. The level of rent is strongly influenced by the rents in the large non-profit social rental sector, which functions as a trend-setter for rents in the private sector, because the apartments in the social rented sector are considered to be equivalent apartments for the purpose of comparison. This means that even though rents basically are free in the Swedish private rental sector, the use of non-profit housing as a trend-setter leads to an indirect influence of costs in the rent-setting process. See also *Rent Policy in ECE Countries* (1990), p. 48 and Victorin (1979), pp. 233-255.

³With the 1988 Housing Act, vacancy decontrol has been introduced to the market in the United Kingdom. Two new kinds of tenancy have been introduced: Assured tenancies (with security of tenure but no right for the tenant to challenge the contractual rent), and assured shortholds (without security of tenure, but with a right to challenge the rent). In both cases, a demand for rent increases is limited to the market rent, see Lewis (1988), p. 893-894. Furthermore, the housing situation has changed dramatically during the last decade. A large part of the council housing stock has been sold off to tenants; the Thatcher government has followed a policy clearly favorable to private home-ownership, and as a consequence the rental sector in general has been diminishing. However, there is still about 11% of the total housing to be found in the private rental sector, see *Rent Policy in ECE Countries* (1990), p. 22.

Ireland the Rent Act was considered unconstitutional in 1980.⁴ In the Netherlands landlords can only terminate leases if they compensate the tenant.⁵ In France and the United States the picture is unclear with various regimes, which are applied to different tenants.⁶ However, it can be said in

⁴Ireland had a very strong rent control regime until 1982. Basically rents were frozen, and no review of rents was allowed. In 1982 and 1983 two new acts were enacted after the supreme court's decision in *Blake-Madigan vs. Attorney General* ruled the old rent control regime unconstitutional, [1982] Irish Reports 117.

The present Irish regime is quite similar to the British regime as it was before the 1988 housing act. Rents are limited to *fair* rents, which must be seen in connection with the quality of the property, the parties' situation, etc. Rent officers and rent assessment committees decide on the level of *fair* rents, see also n. 1 and Ch. 3 n. 12.

⁵In the Netherlands security of tenure is almost absolute, as tenants only can be evicted under extraordinary circumstances. In the case where a landlord wants to use the property himself, eviction is restricted to situations where he has owned the house for at least three years, where the tenant is able to find comparable accommodation elsewhere, and where the landlord pays some kind of allowance for removal costs. Rent increases in the Netherlands are decided politically every year with a rent-price increase trend, which indicates the maximum rent increase, see *Rent Policy in ECE Countries* (1990), pp. 27 and 46.

⁶In France some property dating from before 1948 is subject to strong rent control, while from 1982 *Loi Quillot* changed the rent control regime drastically for the rest of the market; it imposed a somewhat Swedish model, where rent increases were subject to general negotiations between the interest groups. However, this system did not work very well and the system was changed again in 1989. According to the French regime, rents can be negotiated freely, and contracts last for periods of 3 or 6 years. However, security of tenure is at the same time acknowledged to be a very important issue in French law, and the landlord is under obligation to renew the contract if he has no serious reason to reclaim the property, see *Rent Policy in ECE Countries* (1990), p. 44 and de Moor (1983), pp. 425-431.

In the United States the picture is somewhat diffuse. Rent control is enacted either at state level or at municipal level, which means that rent control does not apply everywhere, and where it applies, it is not within the same legal framework.

New York City has a long and unbroken tradition of rent control. It is a system, where tenants are treated depending on which rent control they are under. Old tenants enjoy the most rigid rent control, while another system applies to tenants with new contracts. Moreover, rent control

general that there has not been any clear tendency towards more or less rent control, as the picture varies greatly from country to country.⁷

The Danish legal system

The Danish housing market is dominated by a large market for private home-ownership. More than 50% of the entire housing stock is owner-occupied, and the rest of the market is roughly divided between the private and the social rental sector.⁸ The private rental sector is mainly to be found in the old housing stock in the urban centers, and there is almost no new construction in this sector. As a result, the private rental sector consists of the oldest houses, and the houses in the poorest condition.⁹

One type of housing which is becoming increasingly important in the Danish housing market is housing under a multi-ownership scheme. It is a cross between the private rental sector and condominiums. Legally the tenants form a society, which buys a property. Tenants have a share in the society and with the share also the right to use their individual apartments. This sector is growing both through new construction, as multi-ownership properties receive

does not cover the entire market, and it is combined with vacancy decontrol, see Moorhouse (1987), pp. 20-22.

Some Californian jurisdictions have gained attention for newly imposed rent control programs, and through the last decade some 200 new jurisdictions have imposed rent control, see *supra* Ch. 1, n. 37. Against this background, a tendency towards more rent control can be seen in the United States.

⁷For a short overview of the legal frameworks in Britain, France, Germany, the Netherlands, Denmark and the United States, see also Harloe (1985), pp. 359-383.

⁸Rent Policy in ECE Countries, p. 16 and Wynn (1984), pp. 178-219.

⁹Boligmasse og boligkvalitet (1990), p. 73.

subsidies, and through conversion, because tenants have a right to pre-emption.¹⁰

In the private rental market, rent control is prevalent, and the system is based on cost controlled rents. Contracts are normally made for an indefinite period of time; landlords can only make contracts for a limited period of time if they have a special reason to do so, and it is virtually impossible for landlords to evict sitting tenants.

Danish landlord and tenant law is regulated mainly by two acts -- the Rent Act and the Rent Restriction Act. The acts are amended quite often, although the

¹⁰Tenants under a multi-ownership scheme do not pay rent according to the rent law, but they pay a subscription to the society, according to a decision made by the general assembly. However, many provisions from the Rent Act apply to these dwellings, e.g., the right to sublet and the right to swap, see *infra* p. 88.

Property under this scheme can be sold, but only at regulated prices where the shares are sold at the book value, with adjustment for the actual value of the house, i.e., the value as a private rental house under rent control, and the value of individual improvements made by the owner in the property. The market is not very well organized, as the societies themselves control prices. Principles for valuation of improvements vary largely from society to society, and prices are rising very fast in some societies.

Even though there are some similarities between condominiums and multi-ownership property, the markets function independently. The purchase of multi-ownership apartments is financed only through 10 year loans, and there is no open market. Because prices are controlled, buyers can usually be found easily. Condominiums, on the other hand, are considered to be real property on its own; prices are free, and they are financed by mortgages. Moreover, the legal bases for the two are completely different. Condominiums are exactly described and owned as such, while it is quite unclear what shareholders under the multi-ownership scheme actually own, as the share size, the dwelling size and the contributions not necessarily correspond. Condominiums are subject to lovbekendtgørelse nr. 601 af 21/8 1990 and rights over condominiums are registered in the land register. Multi-ownership apartments are not registered but only subject to Lovbekendtgørelse nr. 361 af 25/7 1985, which is mainly concerned with regulation of prices. The description of the rights of an owner follows only the laws of the multi-ownership societies. See also and *infra* Ch. 4, n. 52.

two last major changes were in the seventies, when the present regime was introduced.

Apart from the two main acts, there are some other acts of importance to landlord and tenant law such as the Fire Precaution Act, the Forced Administration Act, the Rent Subsidy Act, the Condominium Conversion Act and the Act Concerning Houses under a Multi-Ownership Scheme. These acts fulfill special purposes, and they will not be described here as they are marginal to the issue of rent control.

The Rent Act is the general act of landlord and tenant law, which means that it regulates the contract between the landlord and the tenant.¹¹ It contains all special conditions from the law of contracts, i.e., all special conditions that apply to tenancy agreements.¹²

As a consequence, the Rent Act contains many sections which deal with quite technical contractual aspects of the rent agreement such as how the tenant can

¹¹Lejeloven (The Rent Act) is universal. As opposed to the Rent Restrictions Act it applies to all agreements concerning the letting of houses or rooms in houses, regardless of where in the country and no matter for which purpose. All contracts from the subletting of a single room in an apartment to the long-term lease of an entire office building, from a two week holiday house to social housing is included under the law. The law does, however, not apply to mixed contracts where rent is the least significant part, e.g., business leases, where not only rooms but also goodwill and equipment are leased. Neither does it apply to open land, nor to special relations where rent is not paid.

¹²As a principal rule, the Rent Act -- like other Danish acts concerning special types of contract -- is not binding for the parties, and they are free to agree on other conditions than those set up in the act. The act is merely meant to help the parties in shaping a complete agreement, as the order of contract set up by the act will be binding for the parties if they have not agreed on anything else.

However, the axiom that the parties are free to enter any contract they want is far from reality when it comes to rent law, because many sections of the act have been made invariable.

use his dwelling, where and when the rent must be paid, how the heating must be paid, etc. On the other hand, general issues that apply to all contracts such as questions of sanity, age, power of attorney, fraud, definition of defects, etc., cannot be found in the Rent Act.¹³

A large number of sections within the Rent Act have been made invariable, so the parties cannot modify the model clauses set up by the act, or they can only be modified in favor of the tenant. Most of the conditions that could be changed in favor of the landlord have been made invariable, and there is very little room left, despite the freedom of contract, to agree on any conditions that give the tenant a position worse than that set up by the law.¹⁴

While the Rent Act is mainly concerned with contractual issues, the other main act, the Rent Restriction Act, is mainly concerned with economic issues, or rent control.¹⁵

¹³Such general issues are described in other acts, e.g., the Agreement Act, no. 242 af 8.5.1917, the Majority Act, no. 554 af 16.11.1976. Moreover all general principles of contract law also apply in rent law.

¹⁴At the same time The Danish Rent Act is very detailed. It consists of the following 19 parts: 1. The application field of the act. 2. The tenancy agreement. 3. Defects in the dwelling. 4. Maintenance. 5. The tenants use of the dwelling. 6. Payment of rent. 7. Payment for heating, etc. 8. Change of contractual conditions. 9. The landlord's access to the dwelling. 10. Improvements, etc. 11. Tenant democracy. 12. Transfer of the tenant's rights. 13. Termination. 14. Cancellation by the landlord. 15. The move out of the tenant. 16. The obligation to offer the house to the tenants. 17. Mediators at the letting. 18. The housing court. 19. The provisions regarding the act coming into force, etc.

This list is meant to give an idea of how the Rent Act models an agreement between parties, and for residential dwellings it makes little difference whether they have signed a written agreement, because these questions have already been settled in the Rent Act.

¹⁵Lovbekendtgørelse nr. 525 af 11/8 1986 om midlertidig regulering af boligforholdene.

The present Rent Restriction Act was passed during the housing shortage just before World War II. At that time an "Act concerning a temporary regulation of the housing situation" was passed. This act has been changed beyond recognition over the years; however, it is still the full name of the Rent Restriction Act.

The Danish Rent Restriction Act does not apply to the whole country, but most urban districts with a significant population of tenants are under rent control, and about 95% of all private rented housing in the country is under rent control.¹⁶

The main purpose of the Rent Restriction Act is to set up provisions according to which rent increases can be allowed. It is a cost controlled rent control system, which only allows the landlord to increase rents according to a complicated calculation showing an increase in the costs of running the house.

In such a calculation, there are strict limits to what can be included. As for capital return, the landlord can only charge an amount which was fixed by law in 1975 and has not changed since then. Accordingly, there is not any connection between market and rent. Moreover, the capital return has become a relatively small part of the rent, as there has been no increase since 1975.

Cost controlled rents only apply to rent increases, and the Rent Restrictions Act does not directly interfere with free price formation in the case of vacancy. However, this is only a theoretical rule, as property may not be let with conditions which are more burdensome than the conditions for other tenants in the same building. Accordingly, in a building with more than one apartment for

¹⁶See Karnov (1989), p. 2139 n. 3. Municipalities can decide whether the Rent Restriction Act shall apply, and it is almost only rural areas in which the Act does not apply. New construction has been exempted from rent control since 1/1 1992, see *supra* p. 14.

rent, the rent restrictions apply indirectly, unless all apartments are vacant at the same time.¹⁷ In this way it is a principle of equality among tenants that leads to cost controlled rents also in the case of vacancies. Moreover, tenants can claim a lower rent if the rent exceeds the *value of the dwelling*, which is found by a comparison with other dwellings of similar standard and location. In this comparison, cost controlled dwellings can also be used, and consequently, cost controlled rents indirectly apply to new contracts.¹⁸

Consequently, the Danish rent control legislation can be characterized as a cost-controlled system, where rents both in the case of vacancy and in the case of later rent increases are subject to control. Moreover, the Rent Act ensures a very strong contractual protection of tenants, as the obligations of the parties are described in detail in the act.

The German legal system

In Germany there is a large market for private rental housing of which most has been rebuilt during the period following World War II.¹⁹ The German housing policy has in contrast to the policies of Denmark and Italy put great emphasis on the construction of new housing, and a variety of subsidies have been available for private entrepreneurs wishing to construct residential housing. In turn, a cost controlled rent is imposed on housing that has been publicly

¹⁷Not only rent restrictions can be more burdensome, but other clauses in the contract, e.g., temporary leases as opposed to permanent can be considered as more burdensome conditions. See Karnov p. 2140 n. 18.

¹⁸The Rent Restrictions Act also contains provisions which are meant to ensure that rent restrictions will work. These provisions concern allocation of funds for maintenance, (§§ 18-22), procedure for improvements leading to rent increases, (§§ 23-29a), security of tenure for single rooms, (§§ 30-34), rent control boards (§§ 35-44), and use of dwellings (§§ 45-53).

¹⁹The private rental sector accounts for 42% of the German housing market, see Rent Policy in ECE Countries (1990), p. 18. See also Hallett (1988), pp. 17-48 and Wynn (1984), pp. 55-74.

funded. This cost control applies as long as there is a public mortgage on the property, but when all loans have been repaid, the property can be let with free market conditions. In this way, the German system has succeeded in attracting capital to the reconstruction of the country.

As a consequence, Germany has a large and modern housing stock, but also rents that are higher than in both Denmark and Italy.

The German legal system does not have a strong rent control. Apart from the rent control that apply the publicly funded housing, and which will not be described further, landlords and tenants are free to negotiate the rent in new contracts.²⁰ Rent control applies only in the case of rent increases, and rent increases are allowed up to the market level as rent increases must be substantiated by a comparison with other property in the same area. At the same time contracts are normally made for an indefinite period of time, and tenants enjoy security of tenure, where they can only be evicted, if the landlord has a *just* reason for the eviction.²¹

The basis of German landlord and tenant law can be found in the German Civil Code.²² The Civil Code applies to all kinds of rent. It is mainly concerned with some very general issues in the relationship between landlord and tenants, because it applies not only to immovable property, but also to the rental of movable property, such as cars, animals, etc.

²⁰Even though cost controlled rents apply to a considerable part of the German housing stock, it will not be analyzed here, as cost control is only a temporary measure that applies for as long as there is a public loan on the property. Moreover, landlords accept rent control in order to get public funding, and thus this regime can be seen as agreements rather than regulation. Here, only the general German rent control law will be examined.

²¹Cost controlled rents do, however, apply in the publicly funded sector.

However, some very fundamental provisions such as those regarding security of tenure for residential tenants have been incorporated into the Civil Code, as they are considered to be lasting law. The landlord's right to terminate the contract has been restricted, and termination is only admissible in certain situations, i.e., where the landlord or his family needs the property for their own personal use, or when the property is going to be sold, and the price depends significantly on the presence of tenants.²³ Moreover, a tenant can claim that a termination causes hardship for him and his family, and that he should not be evicted.²⁴

Apart from the Civil Code much substantial regulation can be found elsewhere. The contracts of the parties are subject to the Act on General Business Conditions, according to which tenants are protected against unusual and surprising clauses of contract.²⁵ This makes it difficult for a landlord to add burdensome clauses to the contract. There is also a model contract, but the parties are not obliged to use it.²⁶ A rent subsidy act,²⁷ a prohibition against the change of the use of residential property,²⁸ and some clauses in the Civil Procedural Code according to which eviction of tenants can be postponed on the grounds of hardship,²⁹ should also be mentioned.

²²Bürgerliches Gesetzbuch vom 18. August 1896, (BGB), §§ 535-580a. For a comment see Palandt (1991), pp. 542-609. See also Grunsky (1983), pp. 583-610.

²³BGB § 564b.

²⁴The social clause, (Sozialklausel), BGB §§ 556a-c.

²⁵Gesetz zur Regelung des Rechts der Allgemeinen Geschäftsbedingungen (AGB-Gesetz) vom 9. Dezember 1976.

²⁶Mustermietvertrag 1976.

²⁷Wohngeldgesetz vom 28. Februar 1990. See also Ch. 1 n. 40.

²⁸Verbot der Zweckentfremdung von Wohnraum, Gesetz vom 4. November 1971.

²⁹Zivilproceßordnung vom 12. September 1950.

The economic regulation is subject to the Rent Increase Act.³⁰ When the parties enter the contract, they are free to agree on any rent they wish. The only limitation to the freedom of contract is that the landlord may not exploit the tenant in terms of profiteering, which is a criminal offense.³¹

Rent increases can be demanded once a year, on the basis of the rent paid for comparable property. However, in a 3-year period rent increases are limited to 20%, regardless of developments in the market.³² Accordingly, in a market with fast rising rents, rent increases will only slowly follow market development. In order to support a claim for a rent increase the landlord can either make a comparison with other property or use a survey made by local authorities or associations.³³

Rent increases can also be made as cost increases. Tenants pay separately from rent also costs such as water, heating, chimney cleaning, refuse collection, etc., and an increase in these costs can be passed on to tenants. Moreover, under some circumstances the landlord can demand a rent increase on the basis of increased capital costs, if the interest on a mortgage has increased. However, only interest increases on a mortgage used to construct or acquire the property can be carried on to the tenant, and then only interest increases up to the interest rate at the time of the contract.³⁴

Consequently, the German legal system does not have a strong system of rent control. Rent control in Germany only applies to rent increases, and it is based

³⁰Gesetz zur Regelung der Miethöhe vom 18. Dezember 1974, (MHG).

³¹Wirtschaftsstrafgesetz, 1954, § 5.

³²The 20% limit was passed by parliament in May, 1992. Before there was a 30% limit to rent increases.

³³These surveys (*Mietspiegel*) are made by local authorities according to MHG § 2(5).

³⁴See MHG § 5.

on a market rent. There are only a few elements which serve to keep rents under the market level, and German law seems to concentrate principally on security of tenure.

The Italian legal system

In Italy housing consumption is less than in both Denmark and Germany. The average number of inhabitants per dwelling is 3.2, against 2.3 in both Denmark and Germany.³⁵

However, also in Italy there is a large market for private rental housing, although it is declining. Between Italy's last two censuses (1971 and 1981), rental housing went down from 44% to 35%, as rental housing was either sold off to owner-occupancy or left unoccupied by the owner.³⁶ Moreover, the private rental sector does not seem very well-defined, as it is possible to transfer rental housing into owner-occupancy or holiday homes, and landlords are not obliged to let their property.³⁷

The Italian legal framework for landlord and tenant law is found in the Civil Code. As in Germany the Civil Code covers movable as well as immovable property, and most issues treated are of a very general nature within the law of obligation.³⁸

The private rental sector is subject to the Fair Rents Act, according to which rents are fixed according to a tariff and partially indexed.³⁹ The level of

³⁵Occhiuto (1984), p. 603, Rent policy in ECE countries (1990), p 16-17 and Wynn (1984), pp. 247-280.

³⁶Venegoni (1985), p. 283.

³⁷In the Censis (1981) report, 10% of the dwellings in province capitals were declared to be unoccupied. See also De Vita (1985), p. 160.

³⁸Cod.civ., art. 1571-1654.

³⁹Legge 27 luglio 1978, n. 392. - Disciplina delle locazioni di immobili urbani, (legge n. 392/78).

controlled rents is considerably lower than the market rent. Contracts are made for a minimum period of 4 years and automatically renewed, but there is no general security of tenure, as the landlord can give notice of termination without any specific reason at the end of each 4 year period.

Apart from the Civil Code and the Fair Rents Act there are only a few acts concerning rents and rent control. Some acts have been passed to suspend the eviction of tenants in big cities at the end of their term,⁴⁰ and to delay the eviction of tenants in situations where the landlord wants to use his property for purposes other than residential housing.⁴¹ These acts suspend or delay court actions, and they can be seen as political attempts to ease the general problems of the Italian housing policy, rather than as a part of the legal framework.

There is no model agreement, but a specific approval is needed for unusual and burdensome conditions in standard contracts.⁴²

The Fair Rents Act is the most important act in Italian landlord and tenant law. It was introduced in 1978, as an attempt to establish a permanent rent control regime after a long period of various rent freezes and extensions of contracts by law. Tenants in general enjoyed very low rents, and the introduction of the law was partially motivated by the Constitutional Court.⁴³

⁴⁰Decreto-legge 29 ottobre 1986, n. 708, decreto-legge 8 febbraio 1988, n. 26 and decreto-legge 30 dicembre 1988, n. 551. Misure urgenti per fronteggiare l'eccezionale carenza di disponibilità abitative.

⁴¹Decreto-legge 9 dicembre 1986, n. 832. Misure urgenti in materia di contratti di locazione di immobili urbani adibiti ad use diverso da quello di abitazione.

⁴²Cod.civ., art. 1341-1342.

⁴³Corte Costituzionale, 18 novembre 1976, n. 225. See *infra* p. 61.

The basic principle of the Fair Rents Act is that rents are set according to a tariff, based on the construction costs adjusted using coefficients for age, standard, type of dwelling, city size, location, floor and maintenance. The tariff is quite complicated, but it is possible to calculate the rent of any property in Italy on the basis of the tariff. Construction costs are fixed to a certain amount per square meter and published for every year. Rents set according to the tariff are indexed every year at 75% percent of the consumer price index.

The use of construction costs as a starting point may lead to the assumption that the tariff attempts to emulate the long-term equilibrium, as a reasonable return on buildings of the same kind, if built today. However, as construction costs in the Fair Rents Act are set historically, and indexation is only partial, this assumption can only show the original intention of the legislator.

The minimum period of contract is four years, and it is automatically extended for another four year period if none of the parties takes the initiative to terminate the contract. If the landlord wants to terminate, the tenant can benefit from suspension of court action for eviction, and even when court action is taken the tenant will benefit from a considerable postponement, as legal procedures in Italy are slow.

The Fair Rents Act applies to all tenants, both sitting tenants and in the case of vacancies. However, it does not apply in municipalities with less than 5.000 inhabitants or to dwellings let for short periods, such as to foreigners and holiday houses, and there is a substantial market for short term contracts which is completely uncontrolled.

The Italian system can in short be described as a system of complete rent control, i.e., rent control both in the case of vacancies and in the case of rent increases. The economic idea behind the rent control is arguable, as the inner

logic is not coherent.⁴⁴ At the same time tenants in general do not enjoy security of tenure, as contracts are made for a limited period of time.

Some EEC perspectives

EEC law so far has not had any impact on landlord and tenant law in the member states. There has so far been no initiative to harmonize landlord and tenant law within the community. The question of security of tenure has only been brought up twice in the European Parliament, though other questions related to landlord and tenant law, such as construction industry policy have been taken up by the EEC.⁴⁵ It is not likely that EEC law will have any significant influence on landlord and tenant law in the nation states within the near future. However, there are two trends in EEC law which may influence rent control law in the member states: The free movement of labor and goods, and the harmonization of consumer protection.

The principle of free movement of labor and goods within the Community prevents the member states from maintaining economic or administrative

⁴⁴See Tamborrino (1991), p. 75 and Occhiuto (1984), p. 605.

⁴⁵The first time was in 1985, where a question was asked, (Written question no. 41/85 by Mr. Leslie Huckfield to the commission: Housing - Tenancy rights. Official Journal No. C 255, 07/10/85, p. 16). In the answer, it is said: "The Commission does not in fact have a general housing policy, firstly because housing is not a matter provided for in the EEC Treaty, secondly because it has not felt itself competent to intervene in matters, which are essentially the responsibility of local public authorities and where harmonization has not historically been considered essential to the functioning of the common market. It follows that the questions, for example, of assessing housing requirements or imposing additional responsibilities on housing authorities, do not arise for the Commission." The second time was in 1990, where a resolution was passed, (Resolution on the right to decent housing -- doc. b3-1461/90). The resolution "calls for the formulation of a Community policy on housing and the residential environment." However, no housing policy has been adopted so far. For a recent study, where housing is put in a European context, see Ghekiere (1991), pp. 23-24.

barriers.⁴⁶ In a society with rent control, there is also a housing shortage which makes it difficult to find accommodation in the rental sector. In turn, only some expensive submarkets are easily accessible to foreigners from other member states.⁴⁷ Obviously, nationals and foreigners are hit equally hard, but the point is that mobility is restrained. People coming from outside, either from other cities or countries, are at a disadvantage in comparison with residents who enjoy low rents. At the same time people are reluctant to move, because they will have to give up their low rents.⁴⁸ This argument could be brought forward in a case at the European Court of Justice as a violation of art. 48 and 52. However, such a case has not yet been seen.⁴⁹

Harmonization of consumer protection is an issue in EEC law, and it can be argued that a certain minimum protection is needed for tenants everywhere in the EEC. Such protection could be achieved through a standard model agreement which would ensure that tenants, wherever they went, could expect roughly the same content in a tenancy agreement. However, it is not likely that this is going to be an objective of the EEC in the near future, even though consumer protection is an important field of EEC law. Consumer protection in the EEC is related to the functioning of the common market. As houses are

⁴⁶Treaty of Rome, art. 48.

⁴⁷For example, in Denmark there is a small submarket for letting condominiums or houses on temporary contracts at high rents. In Italy there is a large market for temporary contracts, which are exempt from rent control, according to legge n. 392/78, art. 26, a.

⁴⁸See Albon and Stafford (1987), pp. 57-65. It should also be noted that the validity of this argument has been questioned, see Whitehead and Kleinman (1985), p. 518.

⁴⁹This argument is in line with the right-to-travel approach put forward in some American constitutional cases, see *infra* Ch. 3 n. 54 and Harle (1986), pp. 165-169.

As a more subtle argument, EEC competition law could be used also. This would be in line with the antitrust approach put forward in the US, see *infra* Ch. 3 n. 54.

non-movable, there are not the same considerations to be given as to the free movement of goods.⁵⁰

Consequently, it is not from the EEC that any change in rent control law should be expected. Rent control legislation is likely to be continued at national level, similar to the situation in the United States, where rent control is considered to be a matter of state regulation.⁵¹

The basis for comparison

The Danish, the German and the Italian rent control regimes show distinct differences. The Danish system is an outright cost-controlled system that does not allow any market interference in the price adjustment mechanisms. At the same time security of tenure is almost complete. The German system on the other hand is very close to rent decontrol, as prices can be set according to the free market, and only rent increases are subject to control. At the same time tenants still benefit from security of tenure. The Italian system is based very strongly on tariffs, and rent increases are only allowed as a partial indexation. Meanwhile, Italian tenants do not enjoy the security of tenure that Danish and German tenants enjoy.

Denmark can be seen as the most protective country, as sitting tenants enjoy strong contractual protection as well as protection against rent increases. In Germany there is also contractual protection, but the economic security of tenure is somewhat limited, even though there are some restrictions on how

⁵⁰This can be seen in the Commission's answer *supra* n. 45, where it is said that housing is an area, "Where harmonization has not historically been considered essential to the functioning of the common market."

⁵¹See *supra* n. 6. However, a more universal approach would be needed if the European Court of Justice should find rent control violating art. 48, as rent control legislation covers virtually all jurisdictions in Europe.

high rent increases can be. In Italy on the other hand there is only limited contractual protection, as the tenant has no general right to stay beyond the term of contract. However, at the same time rents are kept at a low level.

CHAPTER 3

CONSTITUTIONALITY

In the process of judicial review, judges decide whether legislation conforms to constitutional law. In this process constitutions are interpreted, and provisions of abstract content are applied in order to confirm or reverse decisions made by legislators. Such legal attack on legislation through constitutional courts is in fact a political attack which is launched by lawyers. Constitutional courts cannot claim to know the constitution better than parliaments. They cannot either pretend that they apply constitutions in the only possible way, and accordingly the role of constitutional courts will be seen as the role of political bodies competing with legislators for power rather than as the role of judicial bodies.¹

Obviously, the role of legislators is more active than the role of constitutional courts, because they have the initiative to legislate, while courts must limit their activities to the review of existing law. As a consequence constitutional law will not be seen as law but rather as politics, and the substance of constitutional court decisions will be seen as expressions of political objectives, which restrain legislators.

¹According to Ross any issue of constitutionality is a political issue, see Espersen and Ross (1983), pp. 176-179.

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In rent control law the issue of constitutionality arises in two different ways: first as a matter of the landlords' property rights, second as a matter of the tenants' right to security of tenure.²

The landlords' property rights are a variety of rights. They are closely connected with *ownership*.³ Constitutional provisions concerning private property are far from unambiguous, as they protect property rights without specifying what property rights are.⁴ Accordingly, it is left to legislators and constitutional courts to decide which inroads on the landlords' property rights would be unconstitutional.

In rent control law the argument of constitutionality is either aimed directly at the control of rents, contesting the limitations to the landlord's economic use of his property, or aimed at the security of tenure, claiming that the ban on evictions following rent control should be considered as expropriation, because it does not allow the landlord to regain possession of his property.⁵

²Private property is protected according to the Danish Constitution, art. 73, the German Constitution, art. 14 and the Italian Constitution, art. 42.

³See also *supra*, p. vii.

⁴The Danish Constitution, art. 74 reads: "(1) The right of property shall be inviolable. No person shall be ordered to cede his property except where required by the public weal. It can be done only as provided by Statute and against full compensation.. (2) .." The German Constitution, art. 14, reads: "(1) Property and the right of inheritance are guaranteed. Their content and limits shall be determined by the laws. (2) Property imposes duties. Its use should also served the public weal. (3) .." The Italian Constitution, art. 42 reads: "Ownership is public and private. Economic commodities belong to State, to public bodies or to private persons. Private ownership is recognized and guaranteed by laws which prescribe the manner in which it may be acquired and enjoyed and its limitations, with the object of ensuring its social function and render it accessible to all. .." (Translations quoted from Blaustein & Flanz (1987 and 1991), *Constitutions of the Countries of the World* (New York: Oceana Publications).)

⁵In both cases, the discussion about expropriation will focus on questions of expropriation, i.e., whether a rent control legislation can be said to be a general regulation of property rights or a

The tenants' right to security of tenure is a right to a home.⁶ When this right is seen as a constitutional right, it is argued that landlords cannot evict tenants for arbitrary reasons, because such evictions would violate the tenants' right to security of tenure. In this way the tenants' right is seen as a right of its own, which should be protected legally, and thus a constitutional right which applies directly to the contract of the parties as an invariable provision.⁷ Such right should be understood in the context of the principle of the social state, where houses not only serve as assets, but also have a social function.⁸

However, a constitutional right to housing is difficult to define. The constitutional provisions concerning such right are very vague, and when such right is discussed by legal scholars, it is assumed that such right must be balanced against property rights of the landlord.⁹ This balance implies that it is necessary to define, which *just* reasons the landlord can have to evict tenants.¹⁰ This question is not easy to solve at the level of constitutional rights.¹¹

specific transfer of rights from landlords to tenants, and whether the intensity of regulation is so strong that it can be considered an expropriation. See Espersen and Ross (1983), pp. 655-677.

⁶See also De Vita (1990), pp. 35-40.

⁷In some constitutions a right to housing exists, see *supra* Ch. 1, n. 45. However, the content of such right can be discussed, and in both Spain and Portugal, where such right exists, it is not directly enforceable. See also De Vita (1990), pp. 50-51.

⁸See quotations *supra* n. 4. See also Roth (1987), pp. 179-180, where it is concluded that the security of tenure is a constitutional principle, which has found expression through legislation. In Danish law there is no tradition for such perception of social rights as constitutional.

⁹De Vita (1990), p. 36 and Roth (1987), p. 180.

¹⁰See *infra*, n. 34.

¹¹For example, in Germany some temporary measures have been taken to improve the housing situation. These measures include a right for landlords to let out some property that would otherwise not be let on time contracts and without security of tenure. See Gramlich (1990), pp. 2611-2613. This is a political measure, which compromises the security of tenure for

When decisions are made in constitutional courts they are followed by legal arguments. These arguments will be seen as a way to legitimize a political decision, rather than as arguments leading to the decision. In turn it will not be very interesting to analyze the reasoning of constitutional courts, and emphasis will be given to the effect of constitutional court decisions on legislation.

In all three countries rent control legislation has been subject to judicial review to some extent. Even though constitutional practice differs widely from one country to another, and in particular the willingness of the judges to decide on constitutional issues differ, the issue of constitutionality in rent control can be seen as a political limitation to how far rent control can be taken by the legislator in each country.

Though rent control legislation has been examined by courts in all three countries, it has not been found entirely unconstitutional in any of them, although some advice concerning the interpretation of legislation and the need for new legislation has been given by the courts.¹²

some tenants in order to achieve more housing, and thus to achieve another social objective. If the security of tenure is a constitutional right, such measure should be unconstitutional.

¹²Only in Ireland has there been a case in which rent control legislation has been ruled unconstitutional outright by the Supreme Court, in *Blake Madigan v. Attorney General* (1982), I.R. 117.

The Irish Rent Restrictions Act, 1960, of which Parts II and IV were found unconstitutional, applied only to dwellings built earlier than 1941, and only to dwellings with ratable values below a certain level, (Art. 3). The act froze rents to the level of a basic rent, which in most cases were the rent at the time when the act came into force, (Art. 7). In the Supreme Court judgment it is said:

"In the opinion of the court, the provisions of Part II of the Act of 1960 (as amended) restrict the property rights of one group of citizens for the benefit of another group. This is done without compensation and without regard to the financial capacity or the financial needs of either group, in legislation which provides no limitation on the period of restriction, gives no opportunity for

Judicial review in Denmark

In Denmark there is, as opposed to Germany and Italy, no constitutional court. All courts can apply constitutional provisions, and a conflict between constitutional provisions and parliamentary acts is settled according to the principle of *lex superior*. However, there is no tradition at all in Denmark for a judicial review of legislation. It has only happened once that the Supreme Court has found an act unconstitutional, and both in the literature and among judges, judicial review of legislation is rejected as judicial interference in political matters.¹³

review and allows no modification of the operation of the restriction. It is, therefore, both unfair and arbitrary. These provisions constitute an unjust attack on the property rights of landlords of controlled dwellings and are therefore contrary to the provisions of Article 40.3.2 of the Constitution."

Later in the judgment Part IV of the Act, which restricts the landlord's right to recover possession, is also found unconstitutional. It is argued that this part must be seen together with Part II, and thus it cannot stand alone.

The most important arguments against the Act seem to be that the Act is permanent and it gives no opportunity for review, and consequently, the conditions of tenancies remain at a deadlock.

After this judgment, the Rent Restrictions Act, 1960 was substituted by a legal framework based on fair rents after the British model with rent tribunals and rent officers, who can review the rent and decide a fair rent, see Housing (Private Rented Dwellings) Act, 1982 and Housing (Private Rented Dwellings)(Amendment) Act, 1983. See also McCormack 1983, pp. 205-224 and Ch. 2 n. 1.

¹³In the case UfR 1971, p. 299H, the Supreme Court found the act unconstitutional. It was a case concerning the surrender of a collection of Icelandic saga manuscripts to Iceland. The manuscripts legally belonged to a foundation, but they were kept in the Royal Library in Copenhagen. In the court decisions it is said that the act which surrendered the manuscripts was unconstitutional in the sense that it constituted an expropriation. However, at the same time the Supreme Court found that the manuscripts did not represent any economic value which could be compensated. See Sørensen (1973), p. 300-302.

However, there have been situations in which rent control has been questioned from a constitutional point of view.

One of the few cases in which it was argued that a parliamentary act was violating constitutional provisions concerned rent control. The Landowners' Association tried the legitimacy of the rent control legislation in 1965 in the Supreme Court.¹⁴ At that time, various temporary rent control acts had been in force since 1939, and these acts either froze rent completely or allowed only very small rent increases. It was pleaded that rent control, combined with a ban on eviction and an obligation to relet vacant property at controlled rents, was unconstitutional, because the rent control regime did not allow landlords to increase rents to compensate for increasing costs. Moreover, it was pleaded that a general principle of equality was violated, as price increases were allowed in other economic spheres, and thus landlords were placed in a position comparatively worse than other investors.

The High Court found that the act was a matter of general regulation rather than a transfer of property rights to the authorities, and that the ban on evictions and the obligation to relet under rent control were reasoned in the housing shortage arising during World War II. Accordingly, the rent control legislation could not be considered as expropriation.

When the case was decided in the Supreme Court, a new rent control act was under preparation.¹⁵ This new act allowed some rent increases, and in the

There is still today a clear attitude among judges towards the issue of constitutionality. This can be seen in an interview with Supreme Court president Niels Pontoppidan, *Lov og Ret*, November 1991, where a call for judicial review is rejected.

¹⁴UfR 1965, p. 293H

¹⁵This act was later to be passed as the 1967 version of the Rent Restrictions Act. It was intended to lead to decontrol over an 8-year period. However, this intention was never achieved.

judgment of the Supreme Court it is mentioned that this preparatory work was taking place. Accordingly, it seems that the Court attached some importance to the temporality of rent control legislation, though this is not explicitly stated in the judgment. The Supreme Court decided like the High Court, that rent control legislation was constitutionally legitimate.

The Supreme Court decision itself is very short, but it has been commented on by one of the judges, who argues that there is no real difference between rent control and other maximum prices, for example, on foodstuffs, which have for a long time been acknowledged as constitutionally legitimate.¹⁶ Even though landlords were obliged to relet property at controlled rents and thus had no option to opt out of rent control, the judge argued, that such obligation also applies in reality, for example, to farmers, as they have no real choice of *not* selling their products at controlled prices.¹⁷

The case is in line with the Supreme Court's attitude in general towards judicial review, and it may be seen as a part of the political process leading to new legislation, rather than purely as a legal attempt to check rent control.

In the Danish parliament, the question of constitutionality has also been touched upon. In 1975 a permanent ban on eviction of tenants was introduced in Denmark, and at the same time, tenants were granted the right to exchange property, i.e., the right to allocate their property to other tenants on a mutual basis.¹⁸ The act was passed by a large majority in Parliament in the largest postwar compromise on housing in which the present regime of cost controlled

¹⁶See UfR 1965 B, p. 241.

¹⁷See also Espersen and Ross (1983), p. 665 and Sørensen (1973), pp. 405-406 on the decision.

¹⁸This right can be seen as a possibility for tenants to capitalize their tenure, Boligmarkedet og boligpolitikken (1988), p. 27. See also *infra*, p. 88.

rent was also introduced. At that time there was no discussion about constitutionality; in Parliament social democrats praised the new acts for giving new rights to tenants, while the right wing parties saw them as a first step towards decontrol -- allowing landlords to have their costs covered.

In 1986 there was a proposal in Parliament for an amendment of the Rent Act which included an extension of the tenants right to exchange property. According to the proposal, the right to exchange should be extended to tenants in condominiums.¹⁹ On this occasion the question of constitutionality was brought up, and a parliamentary commission asked the Ministry of Justice for an opinion on the matter. The answer was far from clear, but afterwards, the Rent Act was amended without further regard to constitutional matters.²⁰

At the same time tenants' right to exchange was also extended to cover exchange between different sectors of the housing market, i.e., tenants could exchange property with owners of condominiums, houses, property under a multi-ownership scheme, etc.

¹⁹Tenants in condominiums already enjoyed full security of tenure, if they had let before conversion of the house; landlords could only wait for the tenants to move out in order to use the property themselves or to sell the vacant property for owner-occupancy. With the extension of the right to exchange property, tenants and their successors have become able to extend the tenure of such property infinitely.

²⁰Annex to *Tillægsbetænkning afgivet af boligudvalget den 26. maj 1986* (til lovforslag nr. L 182). The Ministry of Justice was obviously reluctant to give an answer. In the response, it was pointed out that the main issue of constitutionality would be the depreciation of condominiums with sitting tenants. It is said that a certain intensity of the effect on ownership is required in order to consider something to be an expropriation, (Espersen and Ross (1980), p. 655), and without any research on the extent of depreciation, the Ministry was unable to decide whether the proposed amendment had such an impact on the value of condominiums that it should be considered as an expropriation. The parliamentary commission was split afterwards, as the right

This led to a very interesting case, which was not pleaded on constitutionality, though this issue was closely related.²¹

A tenant who lived in a condominium in an attractive suburb of Copenhagen, arranged to exchange his apartment for a house in the same suburb. The owner of the house was willing to give the tenant a discount of approximately DKK 200.000 on the price of the house, because he could take possession of the apartment of the tenant. The landlord refused to accept this exchange, and the owner of the house withdrew from the agreement. Afterwards, the tenant sued his landlord for damages, which were calculated as the discount that he would have had if the landlord had accepted the exchange. In the Housing Court and in the High Court the tenant was awarded damages according to his claim, as there was no doubt that the landlord had been obliged to accept the exchange according to the Rent Act. In the Supreme Court the tenant was not awarded damages, because the Supreme Court considered the discount to be a kind of key money, and as key money is illegal, damages could not be awarded. The Supreme Court decision was very short, and the Court does not answer the underlying question, i.e., whether the landlord had been obliged to accept the exchange.²²

wing parties argued that the amendment would be unconstitutional, and the center and left wing argued that this was not the case.

²¹UfR 1990, p. 36H

²²Moreover, the argument of the court seems incoherent, because -- if the landlord had been obliged to accept the exchange -- the tenant would also have been able to enforce his right. In this way he would be able to capitalize his security of tenure, but not to claim damages, when the landlord obstructs the process. On the other hand -- if the landlords had not been obliged to accept the exchange -- the argument should have been that the agreement involved key money, and in this case, the court would be forced to estimate the value of real property.

The case caused some debate, however, as it became clear that an exchange of dwellings between the sectors of the housing market would allow tenants to capitalize their security of tenure, and before the case was decided by the Supreme Court, the Danish parliament had changed the legislation again, so these exchanges were no longer allowed.²³

Though the issue of constitutionality was never mentioned, and the Supreme Court found a pragmatic solution within the Rent Act, it seems that the capitalization of the security of tenure, as it was put forward in this case, was unacceptable from a constitutional point of view. In particular, as it was a case concerning a condominium where the landlord would be able to sell at market price when the tenant left, it became clear that an asset had been transferred from a landlord to a tenant. The Housing Court and the High Court exposed the problem by awarding damages, but the final decision on changing the law was taken by the legislator. In this way the issue of constitutionality was solved by the legislator, though the question was at first brought up in the courts.

There has not been any attempt to bring up the security of tenure as a constitutional right in Denmark. There are no provisions in the Danish constitution concerning such right, and the security of tenure has found expression through legislation for many years. Accordingly, it is taken for granted, and there has been no real need to describe it as a fundamental right. Moreover, such approach would seem awkward as constitutionality is not perceived as a legal issue in Denmark, and it can be seen that Danish courts do not restrain the legislator through interpretation of constitutional law.

²³It would be virtually impossible for a court to decide on the size of a discount if a case were brought by the owner of the house against the tenant, as such decision would include a decision on the right price of the house, and thus indirectly lead to a price regulation on the market for private ownership.

Judicial review in Germany

In both Italy and Germany, constitutional courts were set up following World War II, and the creation of these courts can be seen as an attempt to give more democratic guarantees in order to avoid a repetition of the abuse of power these countries had experienced.

The German Constitutional Court was set up in 1951, as a judicial review was an articulated principle of the new German Constitution.²⁴ It was a new institution in the German legal system, though constitutional review had existed to a certain extent earlier.²⁵ The Court is competent to decide on a variety of matters, which include very politically sensitive questions, such as election disputes and the unconstitutionality of political parties.²⁶

Nevertheless, the bulk of decisions are taken in disputes involving private citizens. This is done either by indirect judicial review, which is the case when a lower court refers a constitutional matter to the Court, or by constitutional complaints, which is the case when individuals -- after exhaustion of all other judicial remedies -- file a complaint directly to the Court. Indirect judicial review is limited to situations in which judges of the lower courts are convinced that a provision of federal or state law is unconstitutional, and these cases are by far outnumbered by constitutional complaints.

The German Constitutional Court has on a number of occasions decided in cases where rent control and the general ban on evictions have been pleaded

²⁴Grundgesetz, § 93.

²⁵Constitutional review has been discussed in German legal theory for long time, and it found some expression in the Weimar Republic, see Kommers (1976), pp. 30-42.

²⁶For detailed analyses of the German Constitutional Court in English, see Kommers (1976) and Kommers (1989).

contrary to Art. 14 of the German constitution.²⁷ These have been cases of constitutional complaint, and the review of the court has not been limited to the constitutionality of the provisions applied by the ordinary court. The Court has also looked into concrete cases, and decided whether the procedures followed by local courts have been in accordance with the principles of the constitution. In this way the Court has so far avoided finding any provision of the rent control unconstitutional outright.

The Court has not only given decisions regarding pending cases, but has also given some general comments on the interpretation of the law. Consequently, the Court has actively guided the interpretation of rent control provisions, and it seems that the Court has given very exact limitations to the extent to which rent control can be taken without violating the constitutional property rights.

In 1974 the German Constitutional Court decided two cases where ordinary courts had refused rent increases on formal grounds.²⁸ In the first case the plaintiff, Ruhrkohle AG owned 60.000 apartments. The company had not provided the necessary information about comparative dwellings with notice of a rent increase. The company was obliged to limit rent increases to cost increases, and at the same time it was contractually obliged to increase rents for all its apartments at the same time, which made it extremely difficult to provide information for the rent increases. The company was thus only increasing rents to a level below the market level, and the necessary information was sent later to the tenants.²⁹

²⁷Art. 14 of the German Constitution (Grundgesetz) is a protection of private property rights.

²⁸The cases are reported together in BVerfGE 37, p. 132.

²⁹The question of content is a way to ensure enforcement of rent control legislation, see *infra* Ch. 4, n. 136.

In the other case the plaintiff had provided some information about comparative dwellings with notice to the tenants, but not sufficient information, according to the ordinary courts.

In the Constitutional Court, it was pleaded both that the rent control legislation as such was unconstitutional, and that the provisions of procedure applied by the ordinary courts were preventing the landlords from obtaining rent increases.

The Constitutional Court found that the legislator must acknowledge both property law and the necessity of social functions equally, that rent control law should be made in a way so it is possible for the parties to find the lawful rent, that a specific provision that excludes the use of termination as an expedient for rent increases as well as rent control, that limits rents to the level of the rent of comparative dwellings are in accordance with the Constitution, and that it is against fundamental principles of justice, when formal rules prevent the parties from finding the lawful rent.³⁰

In this way the judgment on one hand accepts rent control as constitutionally legitimate, but on the other hand, it was against the constitutional guarantee of private property when the judges enforced rules of procedure in such manner that it became virtually impossible for landlords to carry through a rent increase. For the cases in question this meant that the Court, annulled both ordinary court decisions on the grounds of formal procedures without declaring any legislation unconstitutional.

In the decision it is said that property has a social function, and that the rent control law prevents abuse of termination in case of rent increases. In this way the Court acknowledges that not only property rights deserve constitutional

protection, but also the social function of property deserves such protection though there is no attempt to give substance to this declaration.

The court decision seems to concentrate on something slightly different from the issue of constitutionality, namely the interpretation of formal provisions. According to the Court, these provisions cannot be interpreted in a way that deprives the landlords of their statutory rights. However, in the decision itself it is stated that this is not only a matter of formal provisions changing the substance of law, but also a matter of legal protection of the constitutional guarantees of private property, and the interpretation of formal provisions followed by the ordinary courts cannot be justified by the interests of the tenants.³¹

In turn, this may lead to the assumption that a general rent freeze would not be constitutionally acceptable in Germany. A rent freeze was the substantial effect of the interpretation of the formal provisions in question, and the Court argues on a substantial basis against this interpretation.

In other cases the court has followed this line of interpretation of formal provisions in the context of substantial provisions.³²

In recent years some of the most important cases before the Court have involved a landlord's right to terminate contracts. In German law this right has been limited to situations in which the landlord needs the property for his own personal use or for the use of his family.³³ This right of the landlord to regain

³¹BVerfGE 37, p. 148.

³²BVerfGE 49, p. 245 and BVerfGE 79, p. 80.

³³There are some other situations, where the landlord can terminate, see *infra* p. 95.

possession of the property in a situation where he has a *just* reason is seen as a constitutional property right in German law.³⁴

In 1985 the Court decided two cases where this constitutional right was in question.³⁵ In the first case a landlord wanted to terminate the lease of a 7-room apartment in which she wanted to move with her child, though she was already living in a 3-room apartment. The tenants were a married couple living together with the parents of the husband, and they claimed that the parents would not be able to move any more because of their age. The ordinary court had decided that there was no *just* reason for a termination, as the landlord already lived in a 3-room apartment, and the use of a 7-room apartment for only two persons was considered as an extraordinary housing consumption, and thus not *just*.

The Constitutional Court accepted this ruling. In the judgment, it is said basically it is an individual matter to decide how one wants to live, but in case of termination the ordinary court has the discretionary power to decide whether a situation can be considered as a *just* reason, and when the ordinary court considers so on the basis of an extraordinary housing consumption, it cannot be criticized constitutionally.

In the second case, the plaintiff was an 89 year old woman who wanted to move from the nursing home where she lived into a 160 m², 3-room, ground floor apartment in her own house. Her daughter was living on the first floor of the house, and the elderly woman planned to live in the apartment together

³⁴The word *just* will be used in italics in the context of *just* reason. Terms as *just* reason or *fair* rent do not make much sense, but they are entirely dependent on the interpretation of these normative expressions. The interpretation of *just* reason varies, and by the use of italics, it is stressed that no substantial meaning is given to the term.

³⁵The cases are reported together in BVerfGE 68, p. 361.

with a nurse, so the nurse and her daughter could take care of her. The ordinary court had decided that she had no need for own use, as she was appropriately accommodated with dignity in a nursing home, and as she was not likely to be evicted from the nursing home, her housing situation could not constitute a *just* reason for her use of her own apartment.

The Constitutional Court did not accept this ruling. It is stated that a *just* reason cannot be made dependent on the landlord's present housing situation; even though the landlord already had a place to live; if this was the case the landlord would never be able to regain possession over her apartment, as long as she had room at the nursing home, and such an interpretation would imply that the landlord was unable to regain possession of her property according to her own will. This interpretation of the term *just* reason for own use would not be in accordance with constitutional property guarantees.³⁶

The two cases are concerned about different matters, though both are about *just* reasons for termination. The first case introduces a criterion, which allows courts to balance the interests of the parties, and limit the scope to own use not to include extraordinary housing consumption. The second case discards a criterion, which would require the landlord to be dependent on external factors in order to evict his tenants.

The social function of housing has been mentioned in the argumentation of the Court also in these cases, but no principle of constitutional law is presented in order to give the security of tenure a special constitutional status. The principle of *just* reason seems to be elaborated much more around the landlords' property rights than the tenants' social rights as the entire argumentation

³⁶See comments on the case by Professor Dr. Hans Schulte in *Juristenzeitung* 1985, pp. 528-532.

concentrates on property rights. Even though the Court has acknowledged the necessity of social functions of property, it seems difficult to describe which social functions are constitutional rights in German law, as they do not find any substantial expression in the judgments of the Court; they are only seen as something abstract which is balanced against the property rights of the landlord.³⁷

These cases seen together show how the German Constitutional Court actively interprets rent control legislation. Rent control law is found constitutional, but at the same time the Court gives guidelines for the interpretation of the law.³⁸ In particular in the cases concerning eviction, it becomes clear that the Court through interpretation actively changes legislation and gives substance to *just* reasons.³⁹

In this way, the issue of constitutionality has become very important in German landlord and tenant law, and with Constitutional Court decisions on two of the key issues, namely rent increases and evictions, German rent control law seems thus to be shaped as much by the Court as by the legislator.

³⁷However, it has been argued the such right exists not only as political objectives, but also as legal rights with a substantial content. See Roth (1987), pp. 176-180.

³⁸The cases reported in BVerfGE 37, p. 132.

³⁹The cases reported in BVerfGE 68, p. 361. See also BVerfGE 81, p.29 about termination. In this case a landlord, an innkeeper, had a house with 4 apartments. Three of the apartments were let as holiday homes in connection with the inn. The landlord wanted to terminate the lease of the fourth apartment in order to provide a home for his daughter and son-in-law, who were working at the inn. The ordinary court had found that he did not have a *just* reason for termination, because there were three other apartments in the house which were vacant. However, the Constitutional court found that, if the landlord had to use one of the holiday homes to house his daughter, his business activities would be restrained, and that would be unconstitutional.

Moreover, the activity of the Court can be seen as a sign of the legislator and the lower courts moving very close to what will be the constitutional limits to rent control law. The Court has found it necessary to define the property rights of landlords on two of the key issues while tenants constitutional rights are only described vaguely by the court. This may be seen as a reaction to a social trend towards more security of tenure, as the Court apparently sees property rights as endangered while social rights prevail.

Judicial review in Italy

The Italian system of judicial review is somewhat different from the German system. As in Germany, the Constitutional Court was set up following World War II, but it was only in 1956 that the court started to work. The Court largely handles two kinds of cases, state-regional conflicts and indirect judicial review. Most of the cases which are brought to the Constitutional Court are cases of indirect judicial review; private citizens do not have a right to file direct constitutional complaints as in Germany. However, Italian judges seem to be more willing than their German colleagues to present the Court with cases for review, and in the field of landlord and tenant law the Court has decided in more than 100 cases since the Fair Rents Act came into force in 1978.⁴⁰

Most rent control cases are brought to the Court on the basis of art. 3 or art. 42 of the Constitution. Art. 3 states that all citizens are equal, and it is a task of the Republic to remove obstacles that restrain equality and personal freedom. Art. 42 states that private property is recognized and guaranteed by law, and the

⁴⁰In the period 1951-1967, only 454 cases were subject to indirect judicial review in West Germany, while in the period 1956-1969 there were 2576 cases in Italy. The Italian Court struck out 265 provisions against about only 70 in Germany, see Kommers (1971), p. 115. However, it should be noted that direct constitutional complaints in Germany in the same period came to 2527 cases. See also Certoma (1985), pp. 155-157.

law also decides the limitations of property for social purposes. Although art. 3 in particular is brought forward in almost every case before the Court, almost every possible article in the Constitution has been pleaded.⁴¹

Even though the volume of Italian Constitutional Court cases is considerable, the impact of the Court's decisions seems to be smaller than in Germany. The vast majority of cases are dismissed as unfounded or even clearly unfounded, and the Court has not given itself to key issues in the same way as the German Constitutional Court. However, in some cases the Court has taken important decisions.

The Court was one of those taking part in the political process leading to the present Fair Rents Act. Until 1978 there had been various rent freezes and extensions of contracts in force in Italy. Landlords had not been able to increase rents or evict tenants for a long time. In a case from 1976, where some of these temporary measures were questioned, the Court warned that the regime of rent freezes could not be continued infinitely, because this would be a violation of the property rights of landlords.⁴²

In the decision the rent legislation was upheld as it was justified by its character of extraordinariness and temporality. It was stated that the relationship between landlords and tenants should always be a balance between the rights of the parties, and this balance should only be changed in exceptional cases and for social reasons. However, a change should never constitute a permanent reduction of the landlords' ability to enjoy their property rights.

⁴¹In 107 cases concerning the Fair Rents Act from the period 1981-1989, reported in *Foro Italiano*, 22 different articles of the Constitution have been pleaded.

⁴²Corte cost. - 18 novembre 1976 n. 225.

According to the Court, the continuance of temporary legislation would give the regime a character of permanence. In this case it would be necessary for the Court to review the legislation once again, and this way the court issued a warning that could not be ignored by politicians.⁴³

The decision emphasizes temporality, and according to the judgment, it is a decisive element that the regime can be seen as a temporary measure. In this way the case shows two points: First, the landlords' property rights give some limitations to how far rent control can be taken in Italy; second, these limitations depend on temporality, as temporary restrictions can be more intense than permanent ones.⁴⁴

In 1983 the Court decided in a case concerning the tenants' right to security of tenure.⁴⁵ It was pleaded that the tenants' right is a fundamental human right, and that the social function of housing, guaranteed by the constitution, prevents landlords from evicting tenants at the end of the term of contract without any *just* reason.⁴⁶ In this way it was tried to establish a principle of security of tenure at constitutional level, and the decision can be seen as an attempt to give substance to the social clauses of the Italian constitution.

In the decision, it is said that housing is a necessity, which is protected by law, but the Court cannot consider housing as a fundamental human right, according to art. 2 of the Italian constitution. Such legal construction is not in

⁴³See Lazzaro (1991), pp. 19-20 and De Vita (1990), p. 57.

⁴⁴On this point the judgment seems to give emphasis to *temporality*, and in this way the case seems to be in line with the Irish case, *Blake Madigan v. Attorney General*, see *supra* n. 12, and the statement of Justice Holmes in the American case, *Block v. Hirsch*, see *infra* n. 54.

⁴⁵Corte Cost. - 28 luglio 1983 n. 252.

⁴⁶The case was pleaded on art. 2, 3, 31, 41, 42 and 47 of the Constitution. Moreover, French and German law was brought forward for comparison.

accordance with the legal order, where human rights are considered to be the irrevocable basis of human personality, rather than broader and less precise rights. Moreover, the decision also underlines, that there is an area of discretion for the legislator, when social rights can be interpreted. The rights of landlords and tenants must be balanced against each other, and this is a political process, which should not be reviewed by the Court.

The Court decision can be seen as a matter of reluctance to take politically very sensitive decisions, rather than as a clear rejection of the idea of security of tenure as a constitutional right. The social rights are explicitly acknowledged in the decision, but it is left to the legislator to give substance to these rights.⁴⁷

Numerous attacks have been made on the Fair Rents Act on the basis of constitutional property rights, and sometimes lawyers have shown an incredible imagination when pleading cases, but so far the regime of the Fair Rents Act has been accepted by the Court.

In a case from 1988 the provisions concerning eviction of tenants and criminal liability for abuse of eviction were questioned.⁴⁸ It was claimed that the entire Fair Rents Act was unconstitutional on the basis of art. 3, 10, 42 and 47 in the Constitution and various provisions from the Universal Declaration of Human Rights, the European Convention for the Protection of Human Rights and Fundamental Freedoms and the EEC Treaty.⁴⁹

⁴⁷For a comment on the decision, see De Vita (1990), pp. 54-56.

⁴⁸Corte cost. - 9 novembre 1988 n. 1028.

⁴⁹The arguments against the Fair Rents Act were: Article 3: it creates privileges for tenants, and thus landlords and tenants do not get equal treatment. Article 10: Italy does not fulfill its international obligations regarding human rights, etc. Article 42: the property right is diminished. Article 47: landlords are deprived of the right to savings.

However, the Court did not follow the plaintiff, and the Fair Rents Act was upheld. In the decision it is argued that the act will be constitutional for as long as there is a shortage of housing, leaving tenants weak and in need of protection. It is also pointed out that the legislator has the right to intervene in the house market in order to achieve low rents. The Court did not mention the international considerations that were pleaded, and the arguments of the Court seem very general. In this way the Court refused to decide on a politically sensitive matter, also in this case.

In another case from 1988 it was pleaded that the limitation of capital return to 3.85% in the Fair Rents Act was contrary to art. 41 and 42 of the Constitution.⁵⁰ According to the judge referring the case the fair rent was significantly lower than the market rent, diminishing the property right of the owner, and creating privileges for tenants not dependent on their economic abilities. In the judgment, it is stated that the fair rent of property is calculated according to a variety of factors such as location, type, etc. The valuation of real property on which the rent is based is dependent on the same variety of factors, and the parameters chosen constitute a reasonable attempt to balance the diverse interests of landlords and tenants.

The judgment is not very clear on the matter of limitation of capital return, but it seems to presuppose that rents can be set at a level lower than the market level in order to achieve social objectives.

There have only been few cases in which the Italian Constitutional Court found parts of the Fair Rents Act unconstitutional.⁵¹ When this has happened, it has

⁵⁰Corte cost. - 30 novembre 1988 n. 1048.

⁵¹Corte cost. - 11 febbraio 1988 n. 155 and Corte cost. - 18 febbraio 1988 n. 185.

been specific articles of the act which have been in question, and the decisions have not been changing the basis of rent control.

One of the cases extended the scope for application of the Fair Rents Acts, as art. 26 c of the Act was held to be unconstitutional.⁵² According to this provision some property built before the Fair Rents Act came into force were exempt from rent control. This was property built under special schemes and with rents calculated according to the real construction costs and with full indexation. This property had been exempt from rent control in order to allow landlords who had invested recently to have the return on their investment which had been calculated originally. The Court found that this exemption from the Fair Rents Acts created inequality between tenants who basically enjoyed the same benefit, and thus it was contrary to art. 3 of the Constitution.

This case is interesting, because some property was brought under rent control by a principle of equality. This raises a fundamental question about the objectives for rent control. It can be argued that equality among tenants is a further objective of rent control.⁵³ However, in the overall picture of rent control this decision has little importance, because it focuses on equality which is a formal matter, rather than substantial matters such as social and economic rights.

The Italian Constitutional Court decisions do not show a clear policy. Even though the Court has found parts of legislation unconstitutional, and has also

⁵²Corte cost. - 11 febbraio 1988 n. 155.

⁵³Equality has not been discussed as an objective in itself, and it is not considered to be an objective of rent control here. However, also in Danish rent law there is an element of equality present. It was put forward as an argument for control of new contracts when the present regime was passed in Parliament, see *supra* p. 31 and lovforslag nr. 5 af 2/10 1974 with comments by the Minister of Housing.

on one occasion issued a clear warning to the legislator, it seems that the Court is desisting from interference in politically highly sensitive matters such as rent increases and protection against eviction.

The reluctance of the Court can be seen both when constitutionality is approached as a social right and as a property right. The Court underlines the right of the legislator to shape legislation, and thus the Italian landlord and tenant law is not influenced by Constitutional Court decisions in the same way as German law.

At the same time, it can be seen clearly that there are constitutional restraints on the legislator. Property rights are settings limits for how far rent control can be taken, as the former regime was about to be found unconstitutional. The tenants' security of tenure does not set limits in the same way, and -- as in Germany -- the issue of constitutionality can be much more as a problem of property rights than as a problem as social right. However, it must also be underlined, that the Italian cases seem to be formal rather than substantial, as the Court argues on the grounds of temporality and equality, rather than social and economic guarantees.

The issue of constitutionality

The issue of constitutionality varies greatly from country to country. In some countries it is almost nonexistent, while in other countries it is an important issue.⁵⁴ However, in the field of rent control the constitutional issue becomes

⁵⁴Also in American law constitutionality is an important issue. Though this paper is not concerned with American law, the sheer number of lawyers in the United States implies that any legal issue has been carefully analyzed. In the case of constitutionality of rent control, theories have been developed to such a degree of subtlety, that it would be a pity to leave them unmentioned.

Arguments against rent control on a constitutional basis have been divided into 5 different methods of attack. A presentation of these strategies is given by Harle (1986).

The preemption attack is an argument against local rent control on the basis of state law or federal law. It is argued that if a legal matter has already been subject to federal legislation, there is no room left for states or cities to pass additional legislation on the same matter. The legal frameworks on different levels can be seen as incompatible, and even when there is no direct conflict between the frameworks the lowest ranging framework, (i.e., the rent control) is derogated according to the *lex superior* principle. This argument is not seen in European law, as rent control in Europe is imposed at state level, and not by local ordinance. Thus the conflict between levels of law, only appears either in relation to constitutions or EEC law. See *supra* p. 39.

The emergency requirement is not in itself an attack on rent control, but it can be reversed and used as such. The US. Supreme Court stated in one case that if legislation is aimed at a temporary problem, or a situation of emergency, it can be acceptable, even though it could not be upheld permanently. *Block v. Hirsch*, 256 U.S. 135 (1921). See also *Anon* (1987), 1071-1072. In other words, using temporary legislation more rigid rent control can be allowed than in permanent law. In the words of Justice Holmes in 256 U.S. 170: "A limit in time, to tide over a passing trouble, well may justify a law that could not be upheld as a permanent change." When this argument is reversed, the consequence is that if the emergency ceases, the rent control legislation may cease to operate. It is not completely clear whether the emergency requirement is still valid in American law, as some later court decisions argued it has fallen away since *Nebbia v. New York*, (291 U.S. 502) and *Eisen v. Eastman*, (400 U.S. 841).

The taking approach is the classical expropriation approach to rent control. With this approach it is argued that keeping rents below market level constitutes a transfer of property rights from landlord to tenant. This transfer is a taking, because the landlord is obliged to let his property, i.e., the landlord cannot choose to evict tenants and change the use of the property. This condition of not being able to opt out is crucial for the definition of a taking, as is the period of regulation. If a regulation is made for a short period of time, it is less likely to constitute a taking, and thus there seems to be no sharp line between the emergency requirement and the takings approach. See Harle (1986), p. 165, *Manheim* (1989), pp. 938-940, *Tirolerland, Inc. v. Lake Placid 1980 Olympic Games, Inc.* (592 F. Supp. 304, N.D.N.Y. 1984).

The right-to-travel approach is an argument based on the free movement of persons. It is argued that rent control creates a housing shortage which makes it difficult for people to obtain rental housing when they move to a new city. This restrains the right of tenants to travel and to decide where to live. However, in a legal approach to this right, the problem may arise as to

whether the landlord has a standing, because it is only the rights of his tenants that are questioned. The right is similar to the right to free movement of labor within the EEC, see *supra* p. 40. In America the right to free movement between states has been recognized, but the issue of free movement within states has not yet been brought up for the Supreme Court, see Harle (1986), p. 165.

The antitrust approach is a rather new argument against rent control. It is based on the assumption that rent control corresponds to an agreement on prices among suppliers. Such an agreement would be a violation of American antitrust law, and it can be argued the uniform low rents which lead to a housing shortage also deprive tenants from the right to pay more in order to get a choice. However, in the case *Fisher v. City of Berkeley* the antitrust approach was rejected by the Supreme Court, as the rent control was imposed on the landlords and not agreed among them. See 471 U.S. 1124 (1985), Harle (1986), pp. 169-170, Wiley (1986), pp. 157-173.

Some of the American arguments against rent control are interesting also from a European point of view. In Danish, German and Italian constitutional law emphasis has been put on the classical takings approach, though the principle of equality also has been mentioned in Italy.

The emergency requirement also seems to be used in Europe, as the arguments put forward by the Italian Constitutional Court in Corte Cost. - 18 novembre 1976 n. 225 and in Corte Cost. - 9 novembre 1988 n. 1028 are in line with this requirement. In this case, the legislator was warned that the law was becoming permanent, and in the latter, it is said that rent control was constitutional as long as there was a housing shortage. Also in the Irish case *Blake Madigan v. Attorney General*, *supra* n. 12, the matter of temporality seemed decisive. In this context it is also worthwhile noting that the full name of the Danish rent restrictions act is an *Act concerning a temporary regulation of the housing situation*, and though extremely superficial, the illusion of an emergency requirement is still maintained after 50 years. In Germany some traces of temporary legislation can also be found. For many years there were special rent control regimes in the larger German cities, which were imposed on a temporary basis. In Berlin some of these regulations are still in force, see Sonnenschein (1990), p. 17. Moreover, some incentives for landlords to increase the housing stock have been given a temporary 5 year basis, see Gramlich (1990), pp. 2611-2613.

The right-to-travel and the antitrust approach are both arguments from the tenant's point of view. It is worthwhile noting that the constitutionality of rent control can be argued from both sides, as the distortion of the market not only affects the landlord's return on investment, but the tenant's freedom to choose. The right-to-travel approach is particularly interesting from a

very much a political one, because rent control itself is an issue of strong political interest. As rent control is construed as a normative legal framework in all three countries, the constitutional court review becomes a competitor of the legislator in the making of law.

In Denmark there is no tradition for judicial review at all, while in both Germany and Italy a strong review system with special constitutional courts has been established.

As could be expected according to tradition, in Denmark the courts choose not to interfere in the legislative process, and even when there is a constitutional issue in question, the Danish courts are not willing to decide on it. In Italy the Constitutional Court decides on constitutional matters, but it seems to be more reluctant than the German Court to decide on politically sensitive matters, such as the size of the rent and evictions. The German Court, on the other hand, sets guidelines for the interpretation of law, and thus it seems that the German Court not only sets limits as to how far legislation can be taken, but actually also takes part in the legislative process.

It is not possible to draw any substantial conclusions from this constitutional comparison, because the issue is political.⁵⁵ However, in all three countries there have been constitutional questions about rent control legislation, and there have also been some indications of the limits of constitutionality towards property rights. In Germany the Constitutional Court has clearly drawn the line of how far rent control legislation can be taken. In Italy, the constitutional court

European point of view, as the free movement of persons is ensured by the EEC treaty, and a case on this basis could be tried at the European Court of Justice. See *supra* p. 40.

⁵⁵It seems that some Danish provisions, as the right to exchange, would never be allowed in Germany; at the same time termination, which is a very important issue in German law, would not be considered constitutionally in Denmark at all.

warned the legislator that the former regime was about to be unconstitutional. Even in Denmark with no tradition for constitutional review, the issue of constitutionality has been raised in a -- by Danish standards -- sensible way.

In this way it can be seen that the issue of constitutionality restrains legislators in all three countries, and apparently there are some limitations to how far rent control can be taken. These limitations seem more clearly defined in Germany than in Denmark and Italy, but as the decisions are political it would not make sense to seek the substance of these limitations. Instead, decisions can be seen as a matter of counterbalance, where the constitutional courts react if the legislator moves too far in one direction.

The tenants' right to security of tenure is not explicitly acknowledged by the courts. When constitutional cases have been decided, the questions have mainly concerned property rights, and only in one Italian case, the social rights of the tenants have been the main question.⁵⁶

The efforts made to clarify property rights constitutionally, and the vagueness of social rights leaves the impression, that it is the property rights which need constitutional protection, while social rights are acknowledged, but there has been no need to clarify the content of these rights.

This may lead to the conclusion that rent control in all three countries has been taken close to the limits of constitutional property rights, as there have been cases where the limits have been indicated. Moreover, the perception of rent control as a temporary measure also leads to this conclusion. Although rent control legislation today is older than many other legal disciplines, some rent control regimes are still not perceived as acceptable measures of permanent regulation, and in order to allow a legislation that takes the constitutional issue

⁵⁶Corte Cost. - 28 luglio 1983 n. 252.

to its very limits or maybe even beyond its limits, the fiction of temporary legislation is created.

CHAPTER 4

STRUCTURES

In the following analysis of rent control systems, the legal structures will be divided into three: contractual structures, economic structures and enforcement structures.

Contractual structures are the legal structures which are used to describe and regulate the obligations of the parties. A lease is a composite agreement with many conditions and by-obligations apart from the main obligations.¹ Many of these conditions are so technical and incomprehensible that it is impossible to expect any prospecting tenant to adopt an attitude to them when they appear as contract clauses. Moreover, the clauses vary from very technical questions, such as when and how to pay the rent, to key issues such as the length of contract. Some control of these issues is necessary both to keep rent control from being bypassed, and to ensure a reasonable level of consumer protection.²

Economic structures are used to regulate the economic responsibility of the parties in a way that will prevent the market mechanisms from working. The most important question is how to calculate the rent. However, it is not only a matter of how to calculate the rent in a new contract, but also under which circumstances the rent can be increased, for example, increasing costs, increasing comparable rents, increasing income, improvement, etc.

¹See *supra* p. 2.

²See *supra* p. 21.

Economic structures can, however, be viewed from two sides. The first regards the contribution of the tenant, which is mainly the rent; the second regards the contribution of the landlord, which is for the largest part the provision of a property. Even though emphasis is given to the size of the rent, i.e., the contribution of the tenant party, the economic structures can also include a study of the corresponding contribution from the landlord. A property is likely to undergo major changes over a long period of time, due to improvements, maintenance, lack of maintenance, degeneration, gentrification or maybe even demolition. These problems will, however, be treated as enforcement problems, as they also can be seen as reactions to rent control.

The distinction between economic and contractual structures may seem subtle, and sometimes impossible to draw. Contractual clauses have some economic impact.³ At the same time, economic structures are found in conditions either laid down by law or by contract, and thus they find a contractual expression. In this way all issues have both a contractual and an economic side.

However the distinction between the two structures is practical for several reasons.

Landlord and tenant law is traditionally an area within the law of contracts. Without an explicit contract between the parties there will be many general provisions from the law of contract that will apply, for example, the contract is legally binding, a consideration must be paid, etc. From landlord and tenant law there are many special provisions too which apply to the contract, such as when and where to pay, who is responsible for maintenance, etc. As long as

³For example, a right to exchange property or a right to transfer the tenancy to a member of the household will have some value for the tenant when the rent is below the equilibrium, see also Ch. 1 n. 5.

the parties have not agreed on anything else, these general provisions will make up the contract, and these provisions are not dependent on the presence of rent control.

Contractual rent control makes some of these provisions invariable, and consequently, the parties cannot agree on conditions other than those set up by law. It is a very passive interference in the freedom of contract, and if there were only such contractual rent control, the parties would be free to compensate economically for the imposed regime.

Moreover, the reason for this interference is not only to ensure the efficiency of rent control, but also to give some consumer protection through uniformity of contract conditions. Uniformity makes it possible for tenants to compare property, and the contractual control can in this way be compared with other contractual restrictions in favor of consumers.⁴

In this way contractual structures can be seen as independent from rent control, while economic structures would not be there if there were no rent control. They are concerned with the direct effects of a rent control regime, and the distinction between economic and contractual structures can be seen in the legal framework of the three countries.⁵

⁴This is also the case in insurance law, where coverage and clauses to some extent are standardized by law. See for Denmark: Lovbekendtgørelse nr. 726 af 24/10 1986 om forsikringsaftaler.

⁵In Denmark there is a distinction between the Rent Act and the Rent Restrictions Act, which more or less follows this distinction between contractual and economical issues, as the Rent Act contains all the permanent regulations which apply to the contract, while the Rent Restrictions Act is mainly concerned with limitations to the possible rent increase, due to costs or due to improvement. Maintenance is also regulated by the Rent Restrictions Act, as the norms for how much the landlord must set aside for maintenance. See *infra* p. 138.

The last structures, enforcement structures, are not really concerned with rent control, but rather with making the control work. All the best intentions and even the strongest regime of rent control would not work without an appropriate enforcement structure.

Enforcement structures must be looked at in a very broad context.

First, there is a need for information. If tenants and landlords are not familiar with rent control legislation, obviously it will not work. The parties are often ignorant of their rights, and particularly when the rent control regime is complicated, it can be difficult for the parties to find out both whether they are under rent control and have certain rights, and whether the rent is legal.

Second, there is a need for access to cheap and quick litigation; economic and contractual structures are developed with such subtlety that the parties are not likely to be able to find out immediately what is the legal rent or other contractual conditions. Litigation is a very painful process, both to take on and to wait for. Moreover, when a dispute has been settled, the parties also need

In Germany a distinction has been made between the Civil Code (BGB) and the Rent Increase Act (MHG); all permanent clauses concerning the contract can be found in the Civil Code, while the Rent Increase Act only describes how to carry through rent increases. See *supra* p. 35.

In Italy a distinction can be made between the Civil Code and the Fair Rents Act, though in Italian law the Fair Rents Act is much broader than the German Rent Increase Act.

It is worth noting that in both Denmark and Germany the provisions concerning protection of tenants against eviction have been placed in the permanent acts (lejeloven and BGB), while in Italy these provisions can be found in the Fair Rents Act. In both Denmark and Germany the provisions were also originally in the economic structures, but during the seventies they were moved, and this can be seen as a deliberate choice by which security of tenure moves from being a part of the economic structures into being a part of the contractual structures, i.e., in turn becoming a permanent issue of consumer protection. See Paschke (1991), pp. 270-271.

access to execution, either by set-off or by other means. For tenants the prospect of an endless legal action may be a deterrent.⁶

Third, as mentioned a problem arises when the landlords want to escape rent control. This can happen either through lack of maintenance, which will lower the standard of property or by using their property for alternative purposes, for example, to convert them into condominiums, to rent them as office space or to demolish them and reuse the land.

In the following chapters the structures will be described in further detail, and the legal frameworks of Denmark, Germany and Italy will be compared. However, it is worthwhile underlining that rent control legislation must observe all three structures; a rent control regime cannot function adequately according to its economic content, if not incorporated in a contractual structure -- and made enforceable.

Contractual issues

The basic concepts of the law of contracts are the same in all three countries, and need hardly be described here.

The law of contracts is one of the broadest legal fields in private law; it covers all contracts, and it defines some basic principles of contractual relationships. Landlord and tenant law is only a part of this legal framework, as are all other special contracts, for example, purchase, insurance, transport, deposit and commission, and one of the first questions is to define leases as opposed to other kinds of contracts.

⁶In this context, a reasonable security for tenants to get back their deposits and prepayments in case of change of landlord can also be considered as an enforcement problem; if such security does not exist tenants may suffer from a loss in case of bankruptcy of the landlord. See *infra* n. 21.

A lease is a contract according to which one party (the landlord) gives the other party (the tenant) the right to use an object (the property) during the period of contract; the other party pays a consideration.⁷ The definition may vary slightly from country to country; it serves to determine to which contracts landlord and tenant law applies.⁸

Landlord and tenants law is based on the autonomy of the parties. As a starting point, landlords and tenants are free to enter any contract they want. Only when invariable clauses are introduced the basic principle is left, and rent control law evolves.

There is a problem of delimitation, namely to which contracts rent control law applies. In all three countries, rent control is universal; as a principal rule all contracts for residential use are governed by rent control, although some contracts may be exempted from rent control by special provisions.⁹

When this preliminary question of delimitation has been settled, the contractual issues of rent control can be roughly divided into three groups: first, when the contract is entered; second, during the lease period; third, at the end of contract.

Some interesting aspects will be pointed out in each group, and some invariable clauses will be compared and discussed. In this way the protective

⁷In Denmark, lejeloven § 1; in Germany, BGB § 535; in Italy, cod.civ., art. 1571.

⁸Problems of delimitation between different types of contracts can be seen in all three countries. Some kinds of contracts may have an element of rent together with other contracts, see, e.g., Lazzaro (1991), p. 28 and Krag Jespersen (1989), p. 21. However, these problems will not be treated here.

⁹In Italy temporary contracts, social housing and some luxury housing is exempt, (legge n. 392/78, art. 26); in both Denmark and Italy small municipalities are exempt, (legge n. 392/78, art 26 and boligreg.loven § 1). Social housing is also exempt from rent control in Denmark, see boligreg.loven § 4. In Germany, the MHG covers all contracts.

framework will be described, and it will be shown how invariable law provides security of tenure. However, it is beyond the scope of this paper to give a full account of landlord and tenant law in the three countries.

When the contract is entered

When landlord and tenant enter a lease, there are a number of questions to be settled. The parties often sign a written contract of several pages. This contract has often been set up by the landlord, and the number of clauses alone makes it incomprehensible to the tenant. At the same time tenants rarely get the opportunity to negotiate contractual clauses -- or only very few of them. It is an issue of consumer protection to ensure tenants that clauses which the parties are not likely to negotiate, are reasonable to both parties, so tenants are not surprised by unreasonable or unforeseen clauses which are onerous and thus represent a hidden rent.¹⁰

One way of doing this is to apply model contracts. If a model contract is applied, the clauses printed in the agreement may not be invariable, but they give a great deal of information to the parties. When some clauses have been changed in the individual text of a draft contract, it is clear to the parties that some unusual clauses have been introduced. In this way clarity is achieved, though the use of model contracts does not itself lead to substantial changes in landlord and tenant law.¹¹

¹⁰Such clauses can concern matters of no actual importance to the tenant, e.g., grounds for cancellation, form of notice, etc. These will seem unimportant to the tenant, who has no reason to believe that such clauses will become important.

¹¹Contractual rent control may be introduced together with model contracts, but the application of model contracts does not imply that the contractual clauses become invariable.

In Denmark and Germany model contracts are used, although in both countries the parties are not obliged to use the model contracts; tenancy agreements can be made in any way, oral or written.

In Denmark it is a general principle of the Rent Act to set up a legal framework which cannot be changed by contracts.¹² However, any of the parties can demand a written contract. Such a contract must be made using the model contract form, otherwise all conditions which are onerous to the tenant compared to the rent act are void. The model contract does not bring much new matter to the contract; in fact, it is very close to the regime set up by the Rent Act, and it contains many clauses repeated from the act, which to a large extent makes it unnecessary for the parties to look elsewhere to solve their problems.

In Germany, leases for more than one year must be written, otherwise the contract is considered to be a contract for an indefinite period of time.¹³ The German model agreement is, however, only a suggestion to the parties and not a binding form, and the parties are free to use any form they wish. In addition there is a special act, which protects tenants against unreasonable contracts.¹⁴ According to this act, surprising and anomalous standard clauses are void if they have not been emphasized; ambiguous clauses are construed in favor of tenants; a number of specific onerous clauses are void; and generally all unreasonable clauses are void.

In Italy there is no model contract, but as in Germany, there are some clauses in the Civil Code which protect tenants from entering onerous contracts without

¹²See *supra* p. 29.

¹³See BGB § 566.

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explicit approval.¹⁵ Moreover, many contractual issues are covered by the Fair Rents Act, and thus made invariable.¹⁶

The differences between systems may in reality be very small; invariable clauses in Denmark and Italy and protection against onerous clauses in Germany make it virtually impossible for landlords to exploit tenants through subtle contracts in any of the three countries.¹⁷ Nevertheless, the use of model contracts in Denmark and Germany may have an impact on the efficiency of rent control, as model contracts help to inform tenants of their rights, and thus they also become means of enforcement.¹⁸

Another question, which arises, when a contract is entered, is the question of deposits and prepayments. This is an important question, because large deposits give landlords security and in some cases also liquidity. On the other hand, for economically weak tenants a large deposit may be prohibitive, because they simply cannot afford to pay it. In all three countries there are restrictions to the size of deposit charged by the landlord.

In Denmark, deposits and prepaid rents cannot exceed six months rent.¹⁹ In Germany and Italy, deposits cannot exceed three months rent, and in both

¹⁵Cod.civ., art. 1341-1342.

¹⁶According to art. 79 in the Fair Rents Act (legge n. 392/78) the parties cannot agree on conditions more onerous for the tenant than those set up by the act.

¹⁷It should be noted, however, that in Italy there is a widespread use of temporary contracts which are not subject to the Fair Rents Act. In Italian case law it is accepted that a contract clause can stipulate that the contract is temporary and the tenant may not take up residence in the property. Consequently, the contract is not subject to the Fair Rents Act, and such a clause is legally binding for the tenant. See Tamborrino (1991), p. 80.

¹⁸See *infra* p. 128.

¹⁹In Denmark, the parties can agree on either prepaid rents or deposits in the contract. Prepaid rents can be increased when the rent is increased, and thus the prepayments will always correspond to the actual rent; deposits cannot be increased over time, and they remain

countries the landlord is obliged to pay interest on the deposit.²⁰ In Germany the landlord must pay deposits into a separate bank account, and the interest increases the deposit. In Italy the landlord must refund the legal interest to the tenant every year.

Consequently, it can be seen that in Germany landlords cannot make economic use of deposits, as they must be paid into an account; in Italy, landlords can benefit from the liquidity of the deposits, but they still have to pay tenants the legal interest, which is below market interest. In Denmark, however, landlords have the full benefit of deposits, as they are not obliged to pay interest, and they can hold up to six months' of deposit.

Whereas Germany generally has the least restrictive rent control, and Denmark the most restrictive system, it seems to be opposite when regulation of deposits is compared.²¹

The landlord must provide a property during the period of contract. Leases are long lasting and houses deteriorate; this obligation involves an obligation to

the same during the period of contract. However, landlords can keep deposits but not prepayments as security for damages until the tenant has left the property. The tenant is entitled to use the prepayment to pay the last months' rent, while deposits must also serve as security for damages, and the landlord can keep the deposit until the tenant has left in order to secure any claim that there may be. Deposit and prepaid rents can be combined, e.g., the parties can agree on three months deposit and three months' prepayment, but no prepayment can function as a deposit at the same time, and together they cannot exceed six months rent, see *boligreg.oven* § 6.

²⁰See BGB § 550b and legge n. 392/78, art. 11.

²¹However, in Denmark deposits and prepaid rents are protected by law, as tenants' rights according to the rent law can be advanced against new owners of the house, thus a new landlord must not only respect the rent contract, but also prepaid rents and deposits not exceeding six months' rent. In fact this gives tenants' rights security in the property prior to the mortgagees. See *lejeloven* § 7.

maintain the house; otherwise the quality of housing services provided will be diminished. Lack of maintenance will be considered as an enforcement problem, and the maintenance problem will be described below.²²

There is, however, a contractual problem if the parties agree to transfer the maintenance obligation partly or entirely to the tenant. In all three countries, there is a certain freedom for the parties to agree on such a transfer, and in particular minor work such as superficial repairs, wall-papering, etc., are often at the expense of the tenant. As maintenance work can be very costly, there can be a considerable hidden rent in such clauses.

In Denmark, any transfer of maintenance obligations from the landlord to the tenant will influence the allocation of maintenance funds in the calculation of cost controlled rent, and accordingly, it is not attractive for landlords to pass maintenance to the tenants.²³

In Germany, it is an option in the model contract to transfer certain smaller work, for example, painting, white-washing, etc., to the tenant.²⁴ Other work may also be transferred to the tenant, though such clauses must be made clear in the contract.²⁵

In Italy, there is a division of maintenance work between the parties which is contained in the Civil Code, and though the parties in principle are free to agree on clauses which modify the regime of the Civil Code, the Fair Rents Act does

²²See *infra* p. 128.

²³See *infra* n. 102.

²⁴Mustermietvertrag, § 7, Schönheitsreparaturen and § 8, Bagatellschäden.

²⁵See *supra* p. 79.

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not allow contracts which lead to a rent higher than the legal fair rent. Thus, rents must be lowered if maintenance burdens are transferred to the tenants.²⁶

Accordingly, in both Denmark and Italy there is a protection of tenants against a hidden rent increase through maintenance obligations. In Germany there is no such protection, and there is no need for it as rents are free when new contracts are entered. However, tenants are still protected against surprising and unpredictable clauses.

Probably the most important issue when a contract is entered is the period of contracts. In both Denmark and Germany it is a general principle that contracts are made for an indefinite period of time, whereas in Italy contracts are made for a minimum period of 4 years and automatically renewed.

However, there will always be some situations in which the parties need to make a short term contract.²⁷ Such a contract can also be used by the landlord to undermine security of tenure, simply by making short term contracts and renewing them repeatedly. Consequently, these contracts cannot be prohibited, but on the other hand, with complete freedom to decide on the length of contract also create problems. In all three countries, some legislative measures have been taken against the abuse of these contracts, and to prevent short term contracts from watering down the value of security of tenure.

In Italy, contracts are in general not permitted for a period shorter than 4 years; only in special situations in which the Fair Rents Act does not apply at all, can

²⁶For small work at the expense of the tenant, see cod.civ., art. 1609. For the regime of the Fair Rents Act, see legge n. 392/78, art. 79 and Lazzaro (1991), p. 251-253.

²⁷For example, when the landlord lets out his own home, while he has gone away for a limited time, when he needs the property for his children, when they start university, etc., or when the tenant only stays at the location for a limited time.

such contracts be made.²⁸ In Denmark the parties can enter a short term contract, but the tenant can always question such a contract, and the Housing Court can set aside a time limitation if it is not justified with special needs of the landlord.²⁹ In Germany short term contracts are also allowed, but the tenant can claim continuance of tenancy beyond the end of term if the landlord does not have a *just* reason to terminate the contract.³⁰

The effects of these provisions in Germany and Denmark are that the use of short term contracts as a means of escaping security of tenure does not work, and in these cases emphasis is given to the real problem, i.e., whether the landlord can actually terminate the contract and for what reasons. In Italy, however, the contracts to which the Fair Rents Act does not apply at all constitute a possibility for landlords to escape rent control all together.

During the period of contract

During the period of contract, the parties have certain main obligations and by-obligations.³¹ The tenant is obliged to pay the rent, to use the property according to the contract, etc. The landlord is obliged to provide the property, which is agreed upon, continuously, i.e., he is obliged to keep the property from deteriorating by adequate maintenance. Moreover, the landlord may be obliged

²⁸Legge n. 392/78, art. 1. It should be noted that in Italian law, there is a remarkable exception for contracts for temporary use. These contracts are exempt from rent control, according to legge n. 392/78, art. 26, and they constitute a substantial submarket which is completely free. See also *infra* p. 134.

²⁹See lejeloven § 80 stk. 3. As a consequence, these contracts are not often found on the private rental market, because landlords with more property to let will not easily be able to claim such needs. However, these contracts are quite normal in the submarket of people renting out their own homes for a shorter period of time.

³⁰See BGB § 556b.

³¹See *supra* p. 2.

to deliver other services such as cleaning of staircases, provision of heating, etc.

The tenant's obligation to pay the rent is a key issue; if the tenant does not pay, it is a breach of contract, and the landlord will be entitled to *cancel* the contract.³² Cancellation of the contract has -- like termination -- a very large impact on the social situation of the tenant, and in particular under strong rent control the tenant may lose a right of substantial value in this case.³³ At the contractual level, there are some regulations which make it more difficult for the landlord to cancel as a consequence of non-payment of rent.

³²Cancellation is used in the sense of immediate termination on the grounds of breach of contract, i.e., in Danish: ophævelse, in German: außerordentliche fristlose Kündigung, in Italian: risoluzione per inadempimento. In the case of breach of contract the injured party is entitled to enforce the legal effects of breach of contract on the other party. These effects can be one or two of the three: Cancellation, continuance of the contract and damages. However, some insignificant breaches of contract do not allow the injured party to cancel.

Cancellation can be *ex tunc* or *ex nunc*, depending on the kind of contract, and on the circumstances. Cancellation *ex tunc* is not practical in contracts lasting for a period of time as rent contracts, because the parties have fulfilled their obligations in the past. In the example of non-payment of rents, the contract may have lasted for years before the breach of contract occurs, and there is absolutely no reason to apply cancellation *ex tunc*. Cancellation *ex tunc* is normally only used when the breach of contract was already occurring at the time where the contract was entered, e.g., when the contract was negotiated in bad faith.

Cancellation *ex nunc*, differs from termination of the contract, in the sense that it is an immediate reaction to breach of contract; the period of contract ceases immediately, and there is no obligation for the parties to continue performing according to the contract, whereas in the case of termination there is no breach of contract, and the contract is brought to an end only according to its own provisions and the applicable law. See Gomard (1986), pp. 24-32.

³³See *infra* p. 125.

In Denmark a lease can only be canceled due to non-payment after a warning notice has been sent to the tenant, allowing three days time for the tenant to pay.³⁴

In Germany landlords can only cancel the contract when the arrears exceed one month's rent, and after the contract has been canceled the tenant or the social security office can restore the contract, by paying or guaranteeing payment of the arrears.³⁵

In Italy the contract can only be canceled if the arrears are important, i.e., if the rent is more than 20 days late, or if other charges (heating, etc.), which are late, exceed two months' rent. However, also here contracts can be restored on a later stage.³⁶

Consequently, it can be seen that cancellation in the case of non-payment according to Danish law can be undertaken much faster than in both Germany and Italy, and Danish law lacks those social guarantees which have been given to tenants in Germany and Italy to ensure that a contract can be restored after cancellation.

In the case of cancellation of the contract for reasons other than non-payment, there is also a need for some protection of tenants. Such protection exists in

³⁴See lejeloven § 93. Tenants are allowed to make their payments through the mail, and payments are considered to be on time if they are made to any domestic mail office no more than three working days after the payment date, (lejeloven §§ 32-33). A warning notice can only be sent later to tenants, and it must allow the tenant to pay within three days after receipt of the warning notice.

³⁵See BGB § 554. The option to restore a canceled contract is meant only to be used in exceptional situations, and it cannot be used more than once every two years.

³⁶See cod.civ., art. 1455 and legge n. 392/78, art. 5 and 55. The tenant can up to three times in a four year period restore a canceled contract during the eviction process by paying the rent owed with interests and court costs.

Denmark and Germany, where provisions with regard to cancellation for reasons other than non-payment have been adopted.³⁷ In Italian law, only the general provisions of the Civil Code apply in this situation, and cancellation is here limited to serious breach of contract; however, there is no general restraint on the parties' ability to agree on grounds for cancellation, and thus, when it comes to protection against cancellation on arbitrary grounds, the Italian legal framework seems to provide less protection than both the Danish and the German systems.³⁸

Apart from the matter of paying the rent, the tenant is obliged to use the property according to the contract. This obligation involves questions such as how the tenant can form a household, whether he can take up business activities, or whether he can sublet the property or in other ways transfer it to new tenants.³⁹ These issues are important for security of tenure, because the

³⁷In the Danish Rent Act and the German Civil Code, there are positive lists of reasons for cancellation, e.g., noise, neglect, etc. These lists follow the general principles of the law of obligation, and the parties cannot agree on further grounds for cancellation, (Lejeloven § 93 and BGB §§ 553-554b). Moreover, the grounds are couched in such a way so that the immediate breach of contract does not lead to cancellation. Only when the landlord has protested, and the tenant in defiance of the landlord's order continues the breach of contract, can the landlord cancel the contract. In Denmark, cancellation for other reasons than non-payment is only permitted by the courts in very grave cases. At the same time there is a corresponding right to terminate rent contracts on the same grounds as for cancellation, which can be used in stead. By using termination in stead of cancellation, the tenant will get a certain notice to move out.

³⁸Cod.civ., art. 1453-1462. A conclusion cannot be drawn, however, without an in-depth analysis of the application of cancellation clauses. Such an analysis has not been made.

³⁹The house order can also be mentioned, as a question of use of the property, but it is rather an issue between tenants than an issue between tenant and landlord, as a breach of the house order mostly influences other people living in the same house; however, this matter will not be treated here.

lives of tenants change, and in turn, the needs of tenants change, and if tenants cannot adapt their use of property they may be forced to move.

In all three countries the use of the property is an issue that can lead to breach of contract.⁴⁰ Business activities in a property for residential use is a clear case of breach of contract in all three countries, while on the other hand the tenant always is entitled to live with his family. The problem generally arises when the tenant lives with one or more non-related persons, and here the regimes vary from country to country.

In Denmark tenants have an extended right to use their dwelling. Tenants can choose to live with whom they choose;⁴¹ they can sublet a part of their property, and under some circumstances they can sublet the entire property.⁴² Furthermore, tenants can use their property as a trading object, because they have a right to exchange property.⁴³ These clauses cannot be changed by contract.

⁴⁰See for Denmark, lejeloven § 93, stk. 1, litra b; for Germany, BGB § 553; for Italy, if agreed, cod.civ., art. 1456.

⁴¹It is possible, for the parties to agree on special clauses, which does not allow the tenant to share his property with others, but as the tenant is entitled to sublet the property partly for an indefinite period of time, such a clause can easily be circumvented, see lejeloven § 69. Moreover, such a clause would be considered more burdensome than clauses applying to other tenants, see *supra* p. 31.

⁴²The tenant has a right to sublet the entire property in buildings with more than 6 or 13 dwellings, according to lejeloven § 70. The reason for the tenant to sublet must be that of illness or another temporary absence from the property, and the period cannot exceed two years. The tenant must give the landlord notice of the contract and the conditions agreed on. In relation to the landlord the original tenant remains the contractual party, and the original tenant remains liable for any damages incurred through the sublease. In the relationship between tenant and subtenant the rent act also applies.

⁴³In this way tenants who wish to move can transfer their property to new tenants, and in return they take over the property of the other tenants. Thus tenants capitalize their security of

In contrast, in Germany tenants have only a relatively limited possibility to change the use of their property. Tenant cannot sublet without the consent of the landlord, and they are only under some circumstances entitled to take in a cohabiter.⁴⁴

In Italy, tenants are allowed to sublet parts of their property, but not the entire property. However, the clause has not been made invariable, and thus parties are free to agree that subletting should not be allowed at all.⁴⁵ Tenants do not need permission to take in cohabiters.⁴⁶ Moreover, if the tenant uses the property in a way which is contrary to the contract, the landlord must protest within three months after he has learned of the breach of contract, otherwise he loses his right to cancel the contract.⁴⁷

In all three countries there are some provisions which allow the spouse or cohabiters to continue the contract in the case of the death of the tenant. Also in the case of divorce, the divorcees can agree on who is going to continue the

tenure, see Boligmarkedet og boligpolitikken (1988), p. 27, and this right to exchange has not been unproblematic, see *supra* p. 50.

⁴⁴According to BGB § 549, the landlord is obliged to give his consent only if the tenant has a vested interest in taking in a cohabiter, and this interest has evolved after the contract was signed.

⁴⁵See legge n. 392/78, art. 2, compared with cod.civ., art. 1341-1342.

⁴⁶This can be seen indirectly from legge n. 392/78, art. 6, in which it is stated that the spouse, the heirs, the parents or the relatives cohabiting with the deceased tenant are entitled to take over the property. Heirs can be heirs by will and thus not necessarily relatives to the deceased, see also Lazzaro (1991), p. 127.

⁴⁷According to legge n. 392/78, art. 80. An absolute time limit of one year from the beginning of the uncontractual use was found unconstitutional in Corte Cost. n. 185 del 18. febbraio 1988. Though not codified, a similar rule probably applies in Denmark and Germany on the basis of passivity of the landlord.

lease. If they cannot agree, it will be one of the conditions for the court to decide.⁴⁸

It seems that though all three systems have some protective framework, the Danish system gives tenants much better possibilities to adjust their use of the property when their needs change. Security of tenure has been broadened, and allows the tenant to use his property in different ways which were not foreseen by the contract. On the other hand, the German system keeps the tenant close to the original contract, and the Italian system is somewhere in between the two.

In some situations tenants need to express opinions, and though landlords own their houses and thus basically decide what is going to happen to them, there are some tendencies towards the acknowledgment of the tenants right to decide over their own homes. However there are only a few elements of tenant representation or tenant democracy in the three countries.

In Denmark, tenants are allowed to elect tenant representatives in all private rented buildings with more than 13 apartments. These tenant representatives are meant to be the spokesmen for the tenants, and they are entitled to receive information about the administration of the building. The tenant representatives can set up house rules for approval at a house meeting, and they have a right to approve rent increases under certain circumstances, but in general they do not have any influence on the way the building is administered.⁴⁹

⁴⁸In Denmark this right also applies to registered partners of the same sex, which enjoys the same rights as married couples, see lov nr. 372 af 7/6 1989 om registreret partnerskab.

⁴⁹See lejeloven §§ 64-68.

In Germany and Italy, there is no tenant representation.⁵⁰ This lack of tenants' influence on the administration of their buildings does not seem to be in line with a general trend towards more security of tenure, because an element in security of tenure may very well be a right to control your own housing situation.⁵¹

This can be seen in Denmark, where there is a policy leading towards putting tenants in control of their housing situation, as tenants have a general right to preemption. When a landlord sells his property he must offer it to the tenants at the same conditions at which the contract is closed.⁵²

⁵⁰In Italy tenants have the right to vote in condominium assemblies on questions regarding the provision of heat and air-conditioning. See legge n. 392/78, art. 10.

⁵¹In a broader scale, such a tendency towards more influence of tenants on their housing situation can be seen in the move from a private rental sector towards houses under a multi-ownership scheme and in fact also in a growing sector of condominiums. Owners have a right to decide how to use their property, how to maintain it, they cannot be evicted, etc. In fact, much substantial rent law can be seen as attempts to give tenants the same rights as home owners, and economic rent control can be seen as a way to allow tenants to take part in capital gains in the real estate market. See also *infra* p. 123 about the economic value of controlled property.

⁵²See to Lejeloven § 100. This provision applies to all buildings with more than 13 dwellings, and to buildings only with dwellings (and no business activities), when there are more than 6 dwellings. If the tenants choose to buy the property, it becomes a property under the multi-ownership scheme, see *supra* Ch. 2 n. 10, which is a submarket in the housing market. This market is regulated too, as tenants may only sell their apartments at controlled prices, but the building is entirely run by the tenants, who also decide the rent. Indirectly the tenants also buy the houses at a subsidized price, because they only pay the price of the house, as an apartment house under rent control, whereas the value of the house as condominiums would be much higher.

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Termination

When leases last for an indefinite period of time, as they often do in Denmark and Germany, they continue until one of the parties decides to terminate the lease. It is not possible for the parties to foresee, when and why the contract will be terminated, and the termination of the contract is obviously the core of the question of security of tenure; it is the tenant's right to stay in his home.⁵³

In Italy contracts are made for a definite period of time, minimum 4 years, and at the end of the 4 year period the contract is automatically renewed for another 4 year period, if none of the parties decides to terminate the contract. Such contracts also exist in Denmark and Germany, but they are not common as in Italy, and thus the problems of Italian contracts are to an extent different from Danish and German contracts, though the framework is still comparable.⁵⁴

⁵³See *supra* p. 17. Also, here the distinction between termination and cancellation should be emphasized. Termination is here considered only to be ordinary termination, while early termination is considered to be cancellation. The latter is from a legal point of view completely different from the former, as cancellation is a consequence of breach of contract, and thus it is provoked by the other party. There are not the same needs for legal guarantees in the two situations. Consequently, termination is the manner in which a legally binding contract is brought to an end according to its own provisions or the legal framework which applies, see *supra* n. 32.

⁵⁴The termination issue has also another side. Sometimes tenants want to terminate their contract, and especially in Germany it is quite normal that the rent contract also involves an obligation for the tenant to stay for a certain time, and thus the contract provides a security of income for the landlord. This issue does not involve the same aspects of social obligations as the tenant's security of tenure; it is a mere economical obligation imposed on the tenant, which can be burdensome.

Though it should be a problem under rent control, where most landlords are happy to see their tenants leave, some regulation has been made in order to ease the burden of the contract in all three countries. In Denmark, the landlord is obliged to relet the property as soon as possible, and subtract the rent from the new tenant in the claim against the old one, see *lejeloven* § 86; in

There are two ways to consider this problem. First, how can the tenant extend the contract after the end of term. Second, under which circumstances can the landlord terminate a contract made for an indefinite period of time -- or for a definite period of time, but before the end of term.⁵⁵

In Denmark, tenants have no right to extend their contract beyond the end of their term. On the other hand, time limitations can be disregarded by the Rent Tribunals, and thus there is no need for a right to extend the contract.⁵⁶ If the landlord does not have a good reason to make a contract with time limitations, the clause will be found void.

The German approach is slightly different from that in Denmark. The tenant can claim an extension of the contract for a definite or indefinite period of time, if the landlord does not have any reason that he could have used to terminate the lease at the end of the period of contract. In this way the landlord must have a *just* reason for termination, even in case of contracts with time limitations. However, tenancies, which have lasted less than 5 years do not come under this provision.⁵⁷

In Italy tenants have no general right to extend his tenancy, but they benefit from an automatic renewal, which means that if the landlord does not terminate the contract at least six months before the end of the term, otherwise another 4 year period starts automatically.

Germany a tenant can free himself by suggesting 3 substitutes, who are willing to take over the contract, see *Mustermietvertrag* 76 § 6, and in Italy tenants can *for serious reasons* terminate the contract with six months notice, see legge n. 392/78, art. 4.

⁵⁵The two situations differ; in the first situation, the contract simply runs out and comes to an end, and the tenant must be active to extend the contract; in second situation, the landlord must be active and send a notice in order to regain possession.

⁵⁶See *lejeloven* § 80 and *supra* pp. 28 and 83.

⁵⁷See BGB § 564c.

Here a very big difference can be seen in the fundamental framework of security of tenure between Denmark and Germany on the one side, and Italy on the other. Italy does not have security of tenure in the same way as the other two countries. In Italy, the landlord can evict his tenants for any reason every four years, whereas in both Denmark and Germany evictions must be qualitatively defined as *just*.

This is a very important distinction among the systems. In Denmark and Germany, landlords cannot recover property which is occupied by tenants; only if the property is needed for a *just* reason the property can be recovered. Consequently, landlords cannot evict tenants on discretionary grounds such as general dislike, immoral behavior, protests against rent increases, etc.⁵⁸

The *just* reasons for termination are very closely linked to ownership; in both Denmark and Germany, the contract can be terminated if the landlord needs the property for his own personal use, and in Germany also for the personal use of family members.⁵⁹

In Denmark the landlord can terminate leases on one of the grounds mentioned in the Rent Act. Among these, two are particularly interesting: when the

⁵⁸In some situations landlord and tenant live very closely together, and in such situations termination on discretionary grounds is allowed both in Denmark and in Germany, e.g., in two-family houses, where the landlord lives himself, and in rented rooms within the dwelling of the landlord, see lejeloven § 82 and BGB § 564b, (4) and (7).

⁵⁹See lejeloven § 83 and BGB § 564b. It is also worthwhile noting, that both in Denmark and Germany there is some procedural protection of tenants, i.e., a notice for termination must have a certain content, the tenant must have a right to object, etc. See lejeloven § 87 and BGB § 564a.

landlord wants to use the property himself, and when the landlord has other serious reasons to free himself from the contract.⁶⁰

In the case in which the landlord wants to use the dwelling himself, it is a condition that it is for his personal use. Moreover, the termination must be fair regarding the situation of both parties, and the notice period is one year.⁶¹ The court practice in concerning this provision has been quite restrictive, and in general the landlord cannot rely on being able to terminate on the grounds of personal use.⁶²

Also the case of other serious reasons for the landlord to free himself from the contract has rarely been used. Lately the clause has been used by mortgagees to terminate contracts in condominiums and single-family houses, which they have taken over at a sale by order of the court.⁶³

In Germany the right to terminate on the basis of own use is much broader than in Denmark, as the *just* reason for termination can be both personal use and

⁶⁰See lejeloven § 83, litra a and f. The other grounds are related to special situations; if the landlord can document that the building is going to be demolished or reconstructed in such a manner that the tenant cannot stay; if the tenant is the caretaker, he has failed to fulfill his obligations, and the apartment is needed for his successor; if the dwelling is used by a worker and the use is linked to the conditions of employment; or if the tenant breaks the house rules, but not in such a grave manner that the contract can be canceled.

⁶¹According to lejeloven § 84, it must be considered for how long the landlord has owned the building, and what are the possibilities for the tenant to find a new place to live. It should be noted too, that tenancies in condominiums cannot be terminated at all for the personal use of the owner, if the house was converted into condominiums after the tenant moved in.

⁶²See, e.g., UfR 1968 p. 905, UfR 1989 p. 633 and UfR 1987 p. 171.

⁶³In these situations houses have been sold to be occupied by the owner, and the mortgagees have financed the property. The value of such property is significantly lower, when there are tenants in the property, and the mortgagees will not be able to recover the mortgage if the houses must be sold with tenants. See, e.g., UfR 1941 p. 412, UfR 1978 p. 963, UfR 1990 p. 695.

economic use.⁶⁴ The court practice has been guided by the Constitutional Court which in several cases has found the decisions of ordinary courts unconstitutional because the property rights of landlords were neglected. The landlord can terminate for his own use, the use of family members or household members, and the landlord is free to use the right to terminate.⁶⁵

Alternative economic use of property is also a legitimate reason for termination in Germany. However, a contract cannot be terminated on the grounds of economic use only because the landlord can achieve a higher rent, and because he wants to renegotiate the contract. Moreover, the continuation of the tenancy must prevent the landlord from a reasonable economic use of property, and thus lead to significant disadvantages.⁶⁶ Accordingly, the landlord can terminate a lease, for example, to be able to sell the property at a higher price. If the landlord himself, however, has bought the property with tenants, and thus will make a profit out of the eviction of the tenants, it is not considered to be a

⁶⁴According to BGB § 564b, there are 4 examples of just causes: in the case of breach of contract; in the case of own use; in the case of alternative economic use; and in the case of boxrooms that are changed into dwellings. Tenancies in condominiums can -- unlike in Denmark -- be terminated in German law, but only some years after the owner has acquired the condominium.

⁶⁵The Constitutional Court has found that a just reason cannot be made dependent on the landlord's present housing situation, because a consequence of such an interpretation would be that the landlord was unable to regain possession according to his own will, see BVerfGE 68 p. 361, *supra*, p. 56. Also in BVerfGE 81, p. 29, the court stated that a landlord who needed an apartment for his daughter and son-in-law was entitled to terminate a contract, even though the landlord had three other apartments in the same house which he let as holiday homes. According to the Court, the landlord had not to give up the use of these apartments, before he could terminate the contract. The renting of holiday homes was a part of his business, and it would be unconstitutional to require that he should give up any business activities, before being able to exercise his legal right to terminate.

⁶⁶See BGB § 564b (3) and MHG § 1.

reasonable economic use.⁶⁷ The situations in which the landlord can terminate for economic reason are only those, where the landlord would suffer a significant loss if termination were not permitted.

In Italy, as opposed to both Denmark and Germany, there is no way to terminate a tenancy during the period of contract.⁶⁸ The tenant enjoys absolute protection against termination during the 4 year period of contract. This gives a diffuse overall picture of the Italian legal system, as it on the one hand provides absolute security of tenure during the 4 year period, and on the other hand -- in theory -- there is absolutely no security of tenure at all at the end of the period.⁶⁹

When the landlord has terminated the lease, the use of hardship clauses may soften the effects of termination, either by reversing the termination or by delaying the eviction. Such action is taken on the basis of the hardship of the tenant, and thus independently of the *just* reasons of the landlord.

In Denmark such hardship clauses do not exist, but on the other hand, the situation of the tenant has been taken into consideration when it is decided whether the landlord has a *just* reason to terminate the contract.⁷⁰

In Germany, on the other hand, there are more hardship clauses which allow tenants to stay beyond the end of their contract, and after the contract has

⁶⁷This has been the outcome of several court decisions, see, e.g., Landgericht Mainz in Zeitschrift für Miet- und Raumrecht 1986, p. 14 and Landgericht Osnabrück in Wohnungswirtschaft und Mietrecht 1990, p. 81.

⁶⁸In the transitional period after the introduction of legge n. 392/78, landlords were able to terminate old leases on roughly the same grounds as in Germany, according to art. 59.

⁶⁹Some measures to delay evictions and slow court procedures may, however, lead to *de facto* security of tenure. See *supra* p. 37 and *infra* n. 72.

⁷⁰Accordingly a hardship clause would only be a repetition of a guarantee, which already exists. See *supra* n. 61.

been terminated,⁷¹ and in Italy throughout the eighties there have several times been general holds of eviction procedures which were enforced without any individual considerations.⁷²

These hardship clauses blur the effects of termination clauses, because it becomes difficult to see how strong the protection of tenants is, when there are a variety of hardship clauses in addition to the termination clauses. However, in comparison the Danish system has almost absolute protection according to which landlords are rarely able to terminate contracts, while in Germany the importance of security of tenure is obviously acknowledged, and in general tenants are difficult to evict. However, it can be seen that some of the landlord's property rights have taken precedence over the protection of tenants.

Italy is impossible to place in this comparison, because on one hand, when tenants are protected against termination they enjoy a complete protection; on the other hand, they do not enjoy any security of tenure at all when the contract expires.

This difference between the Danish and German systems on the one side and the Italian system on the other may reflect two completely different attitudes to security of tenure. In Denmark and Germany, where provisions protecting tenants against termination were introduced into permanent legislation, security of tenure is taken to be granted to tenants, and a contract which allows the

⁷¹If eviction is permitted on the basis of own usage, the tenant can claim hardship according to BGB § 556a in order to obtain an extension of the contract, and if this is not possible, the tenant can ask for the eviction to be postponed in up to one year according to Zivilprozeßordnung § 721.

⁷²For example, Decreto-legge 29 ottobre 1986, n. 708, decreto-legge 8 febbraio 1988, n. 26 and decreto-legge 30 dicembre 1988, n. 551. Misure urgenti per fronteggiare l'eccezionale carenza di disponibilità abitative. According to these acts tenants could not be evicted temporarily.

landlords to evict tenants would be considered as burdensome.⁷³ In Italy, however, the security of tenure is not perceived as an inevitable right; it is recognized, but only on a temporary basis, and this may lead to the assumption that security of tenure on a permanent basis would be perceived as unconstitutional in Italy.⁷⁴

Security of tenure reconsidered

This has not been a complete account of the many questions raised in landlord and tenant law, but only a description of a few selected questions of special interest. However, it can be pointed out that in all three countries provide some contractual rent control, even though there is no clear overall picture of the legal frameworks. Security of tenure has earlier been pointed out as the most important issue in rent control law, and in all three countries, there is some contractual protection that prevents the landlord from evicting his tenants.

However, other areas which have been considered also enhance the security of tenure. The right to sublet and exchange property in Danish law can in particular be mentioned in this context, but the use of model contracts and restrictions on cancellation can also be seen as ways of enhancing security of tenure, though here there are no clear lines of legislation on these matters in the three countries.

⁷³This can also be seen from a consumer protection point of view. Tenants expect security of tenure, and it is an essential part of renting a home. See *supra* p. 21.

⁷⁴Security of tenure is recognized during the 4 year period of contract and the earlier provisional extensions of contracts, see also *supra* n. 72. This is, however, a very doubtful conclusion, which can be based on the conclusion to Ch. 3. If there is a tendency to take rent control to its constitutional limits, it can be argued that security of tenure has not found its way to permanent Italian legislation, because it would be perceived as unconstitutional.

Denmark in many ways has the most protective system; though it is easy for landlords to cancel contracts compared to in both Germany and Italy, where tenants have a right to restore contracts after cancellation due to non-payment.

Germany has a system which strongly protects tenants' rights to stay in their property, but at the same time tenants can only use the property according to the contract, and thus over a long period of time in which the needs of tenants change, security of tenure may be endangered.

In Italy the picture is also somewhat diffuse. There is no security of tenure as a starting point, because tenants can be evicted at the end of their contract. However, during the period of contract, tenants enjoy very strong security of tenure which leaves absolutely no possibility for the landlord to regain possession of his property. In this way, the system seems incoherent, overprotective and non-protective at the same time.

It is difficult to reach a conclusion on this basis. A trend cannot be seen in the differences between the legal systems. The contractual protection of tenants also provides consumer protection, and this is in accordance with trends in other legal fields, in which consumer protection is becoming increasingly important. This may lead to the conclusion that there is a trend towards more security of tenure.

Such a trend can be supported by an analysis of German Constitutional Court decisions. The court has drawn some very clear lines, showing that in Germany at least it is not possible to deprive the landlord of the right to terminate a lease on the grounds of his own use, and this action can be seen as a reaction to an attempt from lower courts to enhance security of tenure.⁷⁵

⁷⁵See *supra* p. 59.

On the other hand, it seems that in Denmark security of tenure is taken far beyond what could be accepted by German Constitutional Courts, and again this can be seen as a trend, because there has been no legal counterpart to impede the political pressure for more security of tenure.⁷⁶

It is important to point out that the framework for contractual protection of the tenant also has an economic value for the tenant. The loss of his security of tenure not only leads to a disturbance in the life of the tenant, but also to some costs, such as moving, rent increase, etc. Accordingly, when the landlord is allowed to terminate the contract without compensating the tenant, the tenant suffers an economic loss, and this situation can also be construed as violation of the tenant's property rights.

This point may seem absurd, because the tenants' right to security of tenure is normally perceived as a social right, a right to sit which has no value. The protection of tenants provided by rent control law, however, has an economic value simply as right based on a contract, and the better the legal protection the tenant has, the more it is worth.

In this way the differences among the three countries compared can be seen not only as a delicate balance between the landlord's economic rights and the tenant's social rights, but as a balance between property rights on both sides, where tenant living in the property enjoys a privilege of economic value and the landlord who wants to terminate, wishes to recover his property rights in order to cash in on the privilege of the tenant.⁷⁷

⁷⁶Especially the right to exchange property seems to be a right which is incompatible with ownership in German law.

⁷⁷Also the situation where the landlords claim to recover his property in order to use the property himself can be constructed as a way to cash in, because the landlord alternatively would be seeking a place to live in the free market. In this context, it can seem awkward that

Economics

Economic structures of rent control can be divided into two main groups: rent settings, and rent increases. Rent settings are the issue of determination of rents for new contracts, i.e., rent settings at entry to the market. Rent increases appear during the period of contract. It is very important to have this distinction in mind.

Rent settings are a matter of pure price regulation, according to which the parties' freedom of contract is limited. Artificially low rents lead to a shortage of housing, because more tenants are able and willing to pay the rent asked. In turn this leads to a situation in which the contract itself becomes of value in order to compensate for the lack of equilibrium in the contract.⁷⁸

Rent increases are an issue of security of tenure. The tenant is already in the property, and the landlord wants to increase the rent, which is one of the conditions of the contract. In a society without any security of tenure, there is no distinction between rent settings and rent increases, because both parties are free to negotiate, and -- if no acceptable solution can be found -- the landlord can terminate the contract and evict the tenant, who does not accept a rent increase. In a society with security of tenure, the situation is reversed. The landlord cannot terminate the contract, and thus he has no bargaining power when it comes to rent increases; the landlord does not have any right to opt

both provisions concerning own use and hardship clauses put emphasis on the social situation of the parties. The own use clauses assume that it is a fundamental right to live in your own home, and hardship clauses look at the tenant's individual situation. In this way economic rights are redistributed at random. See also for the liberty rights of private property, Anon (1987), p.1085, and for the apportioning of condemnation awards between landlord and tenant, Goldberg et al. (1987), pp. 1086-1092.

⁷⁸See *supra* p. 9.

out, and as a general principle of the law of contracts, he will not have the right to modify the contract either.⁷⁹ Consequently, provisions, which entitle the landlord to rent increases must be seen as modifications to the tenant's security of tenure.⁸⁰

Accordingly, there are two distinctly different economic issues. First, the issue of setting the rents for new tenants, which is one problem. Second, the issue of how rents can be increased for sitting tenants.

Rent settings

The main problem of rent setting is obviously at which level the rent is set. However, this problem is not different from the calculation of rent increases, and thus it will not be treated separately. The techniques used for rent increases also apply to rent settings at a maximum price.

However, there are two problems of rent setting, which do not occur in relation to rent increases, and they will be treated separately: the problem of key money and the allocation problem.

The simplest way to compensate for rent control is through key money. As the rent asked is below market value, the equilibrium will move from being in the contract to being outside the contract, and the value of the contract can be cashed in through key money.⁸¹

⁷⁹See Gomard (1986), p. 25.

⁸⁰Complete freedom for the landlord to increase rents is not feasible; the tenants will need some protection against unreasonable rent increases, otherwise security of tenure becomes illusory, because the tenant can be forced to move out by higher rents. See also *supra* p. 4.

⁸¹See, e.g., Weber and Wiesmeth (1987), p. 59.

Key money is not allowed in Denmark or Italy.⁸² Key money can be disguised in many ways; it can be paid to landlords, to agents or to former tenants, and can be disguised as payment for various goods and services.⁸³

In Denmark tenants have a right to capitalize their security of tenure through the right to exchange property.⁸⁴ This right has been amended to the Rent Act to alleviate the hardship that tenants suffer as a consequence of the lack of mobility in the house market and it can be seen as a kind of key money, because the tenant can actually trade his property and has actually taken over the right to allotment from landlord.⁸⁵

⁸²For Denmark, see lejeloven § 6; for Italy, see legge n. 392/78, art. 79. In Germany there is no rent control at entry to the market, and thus a ban on key money is unnecessary.

⁸³In Denmark this has been foreseen in the Rent Act, so the contract cannot be dependent on other contracts which could involve hidden key money except in the case of a caretaker contract. For example, the landlord cannot insert a clause in a rent contract according to which the tenant must buy some furniture which is in the apartment at a price set arbitrarily by the landlord. Other arrangements which aim at the same result, but without being called key money, are also illegal. See also UfR 90, p. 36H, *supra* p. 50. In order to avoid the abuse of a situation of housing shortage, the operations of mediators are also strictly regulated, see lejeloven § 106. See also Moorhouse (1987), p. 20, where it is concluded that landlords in New York compensate for rent control by letting apartments with furniture.

⁸⁴This right applies to tenants, who have lived in the same property for more than three years. The provision applies to all houses except those in which the landlord lives himself, and where there are less than 7 apartments. See lejeloven § 73, and Boligmarkedet og boligpolitikken (1988), p. 27.

⁸⁵See bemærkninger til lovforslag n. 4 af 2/10 1974, p. 9. The provision has caused some questionable cases in which tenants with attractive property have exchanged them for considerably less attractive property, and landlords have in some cases argued that the exchange had no real content, as one of the parties -- the one moving to less attractive property -- did not intend to use the new property. See also *supra* p. 50.

The allocation problem

The allocation problem can be described simply as the problem that evolves in a housing market with a shortage. More people are willing to pay the asked rents, and people start queuing for property.

The economic way to solve an allocation problem is to raise prices. In a free market the prices function as a discrimination, and it can be argued that no such thing as a shortage exists, as a shortage will lead to higher prices and in turn also to a diminished demand.⁸⁶

Under rent control higher prices cannot appear directly, through higher rents. Sometimes higher prices are obtained indirectly through key money and burdensome contractual clauses, but such escapes from rent control are often not permitted. Instead, other alternative distribution systems start to work, and discrimination is made on a basis other than the price. As the landlord is free to choose his tenants, the discrimination is made by him, and in none of the countries compared is there any public intervention in the distribution of vacant property.⁸⁷ The following four means of distribution can be pointed out: nepotism, screening, queuing and randomizing.⁸⁸

Nepotism is a policy of favoring friends and relatives. Vacant property is allocated through social structures to family members, good friends, friends of

⁸⁶See Albon and Stafford (1987), pp. 27-37.

⁸⁷As the right to a property under rent control has some value, it is obvious that the landlord wants to profit from this right in any legal way. For professional investors such as pension funds the allocation right plays a role in investment, as the pensioners can have benefit from the property. They arrange queuing systems and internal rules for distribution of property. Other public landlords also have some obligation to distribute property according to public policy, and their allocation procedures can be questioned by the public.

⁸⁸See also Ch. 1, p. 9.

friends, etc., and those who seek a place to live must use their social networking abilities in order to find a property. There is nothing illegal in this procedure, as long as the landlord is private, but nepotism is not likely to promote a more fair distribution of property. The people who know landlords, and who are able to use their networking abilities to find themselves a property are often not particularly poor people. These people are often in a position where they could afford to pay a higher rent. Moreover, nepotism discriminates against outsiders, because they do not have any social network in the society.

Screening is a procedure by which the landlord discriminates between prospective tenants either on arbitrary grounds, such as color or sex, or seeks out tenants who are relatively cheap to serve, such as families with no children. Screening is not a procedure which is only found in rent control; however, in a free market screening will be at the expense of the landlord, because he limits the numbers of prospective tenants and thus the demand for his property by the introduction of screening procedures. Under rent control the expense of screening will be carried by tenants, as the landlord will suffer no loss of income. These procedures are not likely to help poor people or people in need of housing, because they will often be expensive to serve or subject to prejudice.⁸⁹

Queuing or establishment of some kind of waiting list system is not commonly used in the private rental sector, because landlords are not obliged to establish such systems, and they must bear the operating costs themselves. Queuing is better known in the social rented sector, where public landlords must apply some kind of fair distribution system which allows everybody to have access to public housing.

⁸⁹See Loikkanen (1985), p. 500-503.

Randomizing is the last means of distribution. This is a system by which one applicant is picked at random among many applicants, or the first applicant gets the vacant property. This is the last resort, and it resembles a lottery. However, the distinction between randomizing and nepotism is blurred, because applicants need to know about vacancies in order to apply, and again those with a well-functioning social network will obtain this knowledge more easily than others.

None of these alternative allocation mechanisms is likely to give a more fair distribution of vacant property than the distribution promoted by the price discriminator in a free market.

Moreover, there are some real losers, who will never be able to enter the controlled market. These are people coming from outside, such as foreigners or simply people from another city. Also people sensitive to screening are likely to lose, and these losers must seek housing in other more expensive sub-markets.⁹⁰

Vacancy decontrol

Some legal systems, such as that in Germany, have no rent control at entry into the market. The parties are free to agree on any rent they want, and accordingly, rent control only applies to sitting tenants; property becomes decontrolled when the tenant leaves, and new houses and vacancies can be let out at market rents.⁹¹ From a legal point of view, there is a big difference between the two types of control; full control (without vacancy decontrol) restricts the original contract, while rent control combined with vacancy decontrol allows the parties

⁹⁰For example in the parallel, free market for short term leases, private home ownership, etc.

⁹¹Denmark also has vacancy decontrol for houses constructed after Jan. 1, 1992, as the Rent Restrictions Act does not apply to these houses. See *supra* p. 14.

to negotiate freely, and only afterwards the parties are restricted from changing the contract.

Under vacancy decontrol there is no incentive for key money, and the allocation problem does not exist, as property return to the market price upon vacancy. However, other economic problems related to maintenance still exist.⁹²

Rent increases

The problem of rent increases is quite different from the problem of rent setting. It occurs when the landlord after some time wants to increase the rent. The landlord can have two main reasons for wishing to increase the rent.

First, the value of the property can have changed as a result of general changes in market conditions. Prices go up as some locations become more attractive, etc. Moreover, the costs of the landlord, taxes, maintenance, etc., increase, and without rent increases the profit of the landlord will diminish. In this situation the property remains the same, and only its value has gone up. If the landlord cannot claim higher rents in this case, he will see the value of his house fall under market level, as a consequence of rents below market level. This problem must be seen together with the length of tenancies, which often last for decades, while cities grow, inflation rises, society changes, etc.

Second, if the property itself has been changed, because of improvements, then its value increases.⁹³ In this case, the landlord wants a rent increase which

⁹²It can be argued that vacancy decontrol creates inequality among tenants in the same building. This argument was put forward in the argumentation which took place, when the Danish Rent Restriction Act was passed. See bemærkninger til lovforslag n. 5 af 2/10 1974, p 11. It can also be argued that the problems of rent control become worse with vacancy decontrol, because the landlord has more to gain from a termination of the contract, and thus landlords are more likely to harass their tenants. Moreover, sitting tenants become immobile as they cannot go anywhere else at the same rent.

corresponds to the improvements done to the property in order to get a return on his investment for the improvement of the property.

In both cases the tenant needs protection. If there is no protection he can be exploited by the landlord, and his security of tenure will be endangered. On the other hand, the landlord needs rent increases, and a total freeze of rents would be a very severe encroachment on the property rights of the landlords, while a hold on rent increases due to improvements would also mean a general hold on the improvement of housing.⁹⁴

When economic rent control is analyzed, three different techniques for control can be found. These techniques are cost controlled, income controlled and market oriented rent controls.⁹⁵

Cost controlled rents constitute a regime in which rent increases are allowed on the basis of the costs of constructing or running the property. This can be done either by allowing the landlord to increase the rent directly according to cost increases, or by allowing the landlord to pass on some of his expenses to the tenants.

Rents related to income are in practice rather rare. An element of income controlled rent can be found in the public policy of rent allowances, where individuals are supported in order to bring their housing expenditure down to a lower level. In the countries compared there are no policies of rent related to

⁹³Such improvements can be made, e.g., through installation of insulated glass units or central heating in old houses.

⁹⁴For the constitutional approach to a rent freeze see the Irish constitutional case, *Blake-Madigan v. Attorney General*, *supra* Ch. 3 n. 12.

⁹⁵See Rent Policy in ECE Countries, pp. 9-12.

income in the private housing market, but some signs can be found in clauses concerning termination.⁹⁶

Market oriented controls or quality-based rents are based on an assumption of what a market rent would be. This is often achieved by a comparison between properties within the same area and of the same standard. However, some more theoretical models do also exist.⁹⁷

In a cost-controlled system some of the expenses of the property are isolated and transferred from the landlord to the tenant. The remainder, which includes the landlord's return on investment, must be set either arbitrarily or market oriented, and how this capital return is calculated is the key issue of rent increases.⁹⁸

⁹⁶In both Denmark and Germany, the ability of the tenant to provide a new dwelling for himself, i.e., his economic ability, must be taken into consideration in case of eviction, when the landlord's and tenant's needs are balanced, see BGB § 556a and lejeloven § 84.

⁹⁷One way of finding the market rent is to seek long term equilibrium by figuring out what would be the market return on the capital invested in the property, if reconstructed. The model aims at the balance point for new investors who enter the house market. Another way, which was found in the British Rent Act 1977, was to exclude the scarcity element when the rent is found. It seems, however, to be a rather arbitrary approach. See Madge (1985), p. 834, Dent and Doling, (1990), pp. 348-349 and Lee (1984), pp. 289-291. The Italian system of fair rents can also be seen as an attempt to find the long term equilibrium, see *supra* p. 38.

⁹⁸It can be argued that tenants also should have a right to a rent decrease corresponding to the landlords right to a rent increase. If the rental value of the property falls, the tenant should be able to ask for a rent decrease. A distinction can be made between properties which lose value due to market changes, and properties which lose value because they deteriorate.

The market changes if an area becomes less attractive. For example, if an area suffers from unemployment and people move away, if the neighborhood degenerates into a slum. In this case tenants are entitled to a rent decrease in the Danish legal system. According to Danish law, tenants can demand rents to be lowered to market value, based on rents for comparable property, see lejeloven § 49. However, there is a very important distinction between rent increase provisions and the corresponding rent decrease provisions in Danish law, as

All three countries compared have an element of cost-price rent in their policies, and in the following, the cost element of rents will first be looked at. Second, the element of capital return, and the principles behind calculations will be analyzed.

Rent increases due to cost increases

There are two ways to apply cost controlled rents. In Germany and Italy, costs are paid separately from the rent, and they are not considered to be a part of the rent. In Denmark costs are included in a budget for the building, and rent increases can be carried through on the basis of the budget. Consequently, in Denmark the budget and thus the cost controlled rent covers all costs that are relevant to the rent, while costs in Germany and Italy are limited only to some of the actual costs. These costs are almost identical in the two countries; they cover provision of services and maintenance of technical installations, such as elevators.⁹⁹

provisions concerning rent decrease are made invariable, even for commercial lettings. Moreover, there is one important distinction between increases and decreases. The landlord needs some provisions to be able to increase the rent when the tenant enjoys security of tenure, because a rent increase is a change of the contract, see also *supra* p. 4. On the other hand -- in theory -- the tenant does not have the same need, because he can use his bargaining power and fall back on his contractual right to terminate the contract if the landlord will not accept a rent decrease. Accordingly, the tenant only needs a right to demand a rent decrease if tenant rights are conceived as something broader than the mere protection of sitting tenants.

In the second situation where the property is deteriorating, the tenant does not need to accept this. The landlord is obliged to keep the property at such standard that his obligations according to the original contract are fulfilled, and thus the tenant can claim both damages and fulfillment of contract in the case in which the standard comes below the agreed level. See also Lejeloven §§ 9 and 19, BGB § 536, cod.civ., art 1575-1576.

⁹⁹In Germany the landlord is entitled to charge costs to the tenant according to MHG § 4; these costs including heating, water supply, outlet, cleaning, refuse disposal, insurance,

There are three cost elements which cannot be passed on to tenants in Italy and Germany. These are maintenance, depreciation and administration fees. These three cost elements are found in Danish rent control, but they have proved difficult to calculate.¹⁰⁰

Maintenance is difficult to define; the distinction between maintenance and improvements is not clear.¹⁰¹ Moreover, maintenance work is often very costly, and major work is not undertaken every year. Consequently, maintenance costs fluctuate, and there is a need to have these fluctuations leveled out. In Denmark, this is done through an account system. Every year, the landlord must allocate funds to the maintenance account, and the actual spendings are deducted from the account. Allocations to the maintenance account can be included in the house budget, and thus passed on to the tenants as costs. However, as the main account is a virtual account, and the landlord is obliged to maintain the building regardless of the balance of the account, there is little

caretaker, garden maintenance, electricity and maintenance of shared installations. In Italy, according to legge n. 392/78, art. 9 heating, air conditioning, cleaning, maintenance of elevators, water supply, outlet and 90% of the expenses for a caretaker can be passed on to the tenants, and also the supply of other shared services can be passed directly to the tenants.

¹⁰⁰See boligreg. loven §§ 7-9. In Denmark the entire regime of the Rent Restriction Act works on the basis of cost controlled rents. Rent increases are only allowed on the basis of a budget showing increased costs; this budget includes taxes, water supply, refuse disposal and other municipal services, cleaning, administration, insurance, depreciation of installations and return on investment. Maintenance is calculated separately, and added to the budget, and heating is paid separately, see also *infra* n. 102.

¹⁰¹Especially when tax matters also are brought into consideration, the definition of improvements becomes unclear. For the definition of maintenance in Denmark and the problems of taxation, see Norsker (1991), p. 67. For the distinction between maintenance and improvements, see *infra* p. 120.

difference between this account system and a system where maintenance is not calculated separately.¹⁰²

Depreciation of installations occurs because the installations of a property have a limited life span even when they are maintained.¹⁰³ Accordingly, landlords need to renew installations, and in the Danish budgets the landlord can include some allocations for the depreciation of installations. Depreciation is added to the budget every year regardless of the state of installations, and the landlord is obliged to renew installations when needed.¹⁰⁴

Administration costs can create problems, though such costs often can be proved easily, because the administration is carried out by a professional administrator who charges a fee for his services. However, administration is often done by the landlord himself, and even when this is not the case, it may be in the mutual interest of the landlord and the administrator, to provide an administration service, which is expensive. In Denmark rent control boards

¹⁰²The account system consists of three accounts, the main account (§ 18), the special account (§ 18b), and the individual account (§ 22). Only the special account is not a virtual account; it is kept with Grundejernes Investeringsfond, a semi-public administration service. The individual account covers only painting, wall-paper and whitewashing inside the apartments. This account is of some importance, because tenants cannot claim to have any work done if there is no money in the account. The allocations to the maintenance account do not cover the actual maintenance cost, see *supra* p. 13.

¹⁰³These installations can be, e.g., heating systems, elevators, antennae, etc.

¹⁰⁴Depreciation of installations is calculated on the basis of a practice in the rent control boards. Rent control boards set up norms for different kinds of installations, both for how much they cost, and how often they should be renewed. For example, appropriation of a central heating system is calculated on the basis of the size of the house in sq. meters, and no distinctions are made between different systems of central heating, etc.

restrict administration costs in the budget to a certain amount per unit.¹⁰⁵ Such a practice may have the effect that it restrains the actual administration costs, because administrators are forced to compete on prices.

Maintenance, depreciation and administration costs are calculated according to tariffs. These tariffs are set either by law or by the practice of rent control boards. However, when tariffs are used, a generalization is made, and thus these cost elements are calculated independently from the actual costs. Even though these are elements in a so-called cost controlled system, they are made independent of costs by the use of tariffs. In this way, the distinction between costs and rents becomes unclear, as cost elements calculated according to tariffs must be seen as rent rather than costs. In turn, the distinction which can be found in Germany and Italy also applies in Denmark, because cost elements which are difficult to calculate are based on tariffs, and thus it is a fiction for the Danish legal system to be described as cost controlled, relative to the German system.¹⁰⁶

In Italy the basic principle of rent setting is a -- somewhat more subtle -- principle of cost control; the Italian *fair rent* is calculated on the basis of the construction costs of the property, and the rent is regulated every year according to the change in the consumer price index. In this way, the *fair rent* is supposed to be a reasonable return on the landlord's initial investment, namely the construction costs.¹⁰⁷ Construction costs are set arbitrarily every year to a

¹⁰⁵In Copenhagen the board has restricted administration fees for 1992 to DKK 1,500, regardless of the number of units or the actual costs. This practice has been approved by the courts, latest in UfR 1992 p. 248H.

¹⁰⁶In Italy tax on real property and insurance cannot be passed to the tenant, and accordingly costs in Italy are more narrowly defined than in Germany and Denmark.

¹⁰⁷See also *supra* p. 38.

certain amount per square meter, and adjusted through a complicated valuation system. In this way, the Italian system is based on a tariff which is set independently from the actual construction costs, and although the system is supposedly a cost controlled system, it cannot be considered as such.

Accordingly, all three systems compared have a cost controlled element which allows the landlord to pass certain costs to tenants. Apart from the cost element there is a rent element, which covers the landlord's return on investment, maintenance and administration costs. Thus the rent element does not only cover return on investment, but also those cost elements, which have been subject to tariffs.

Rent increases due to increased capital return

There are two general procedures to calculated increases on the return on capital. Rents can be increased after an assessment of the property, which is based on empirical evidence, i.e., a comparison with rents of other property, which is the case in Germany, or they can be subject to some kind of tariff, which is the case in both Italy and Denmark. Tariffs can be indexed, either in a part or entirely, which is the case in Italy, or they can be frozen, which is the case in Denmark.

A system of rent increases based on comparative rents simulates a free market. It is a flexible system, which allows tenants to pay according to their actual housing consumption, and landlords to obtain market rents from sitting tenants. The disadvantage of this system is obviously higher rents, and accordingly the security of tenure will be endangered, because rents may increase to a level above the ability of the tenants. Moreover, it can be difficult for the parties to find the correct rent and in turn this leads to litigation.

It is also an important but rather technical problem in such a market oriented system how to decide which properties are comparable. There is a big difference between a comparison with newly let properties, which give the newest status of the market, and a comparison with properties which have been let for some time, which can be used for comparison in order to avoid fluctuations and ensure a continuum of slow price movements.

In Germany, where the comparative rents system is applied, the litigation problem has been reduced by the use of rent surveys,¹⁰⁸ and the problem of continuum has been solved by the use of newly-let property in the comparison, and to avoid fluctuations, rents can only increase by 20% over a 3-year period.¹⁰⁹ This leads to a slowdown in rent increases in Germany, which --

¹⁰⁸See also *supra* p. 35.

¹⁰⁹See MHG § 2, and *supra* p. 35. In the Danish Commercial Rent Act, which is also based on comparative rents, only property which has been let for at least one year can be taken into consideration when rents are compared, (Erhvervslejeloven § 3).

It is also worth noting that Denmark has a system of rent increases on the basis of comparative rents which applies in some situations; the Rent Act contains some general provisions concerning the change in contractual conditions. These provisions have only limited effect on private rental housing, as the provisions are to a large extent substituted by the Rent Restriction Act. However, in certain situations the provisions will still apply, e.g., in non-controlled areas and when tenants apply for a rent decrease, see *supra* n. 98.

Landlords can demand a rent increase if the rent is lower than *the value of the premises*. It is specified in the act that the *value* is found by making a comparison among premises of the same size, type and standard in the area. A rent increase can only be made every second year, and only when there is a significant difference between the *value* rent and the actual rent. The tenants must be given three months notice, and if they protest against the increase the landlord is obliged to take the tenants to court in order to justify the rent increase.

Corresponding to the provisions concerning rent increases, the tenants demand a rent decrease on exactly the same grounds, i.e., if the rent is considerably higher than the *value* of the premises.

together with the delay of rent increases due to the use of the comparative method -- gives sitting tenants the benefit of lower rents.

It can be argued that the German system of rent control in which rents are limited to market rents, prevents security of tenure from becoming of economic value, and accordingly security of tenure is only a social issue. However, there is a maximum level of rent increases, and there is always a delay in the burden of proof, which means that rent increases follow some time behind the market. Moreover, in the legislation it is acknowledged that economic hardship is a reason that tenants can use to claim an extension of the contract.¹¹⁰ So even though rents are not intended to be regulated at a level lower than the market rent, there is a substantial effect of rent control which leads to lower rents.

Tariffs are used in both Denmark and Italy. In the Danish legal system tariffs are used for capital return, maintenance, depreciation and administration costs.¹¹¹ These tariffs are either set by law, which is the case for the first two, or by rent control board practice, which is the case for the last two.¹¹² In Italy the tariff is set by law.¹¹³

The general problem of tariffs is how to set them, as tariffs are set arbitrarily; there is no direct linkage between rents and the actual quality of the property, and tariffs only with difficulty reflect the location of the property, which is very important in free market pricing. In Denmark the capital return on a property is calculated as 7% of the assessment for the taxes on property made in 1975. The assessment was made under rent control, and it was quite low because rents at that time were very low. In Italy the rent is calculated as 3.85% of the

¹¹⁰See BGB § 556a.

¹¹¹See *supra* p. 114.

¹¹²See *infra* n. 143.

¹¹³See *supra* p. 38.

estimated construction costs. In both cases the result is rents which are arbitrarily set at a level lower than the market level.

Rents can be indexed, so they follow the general price level or the price level for some particular goods.¹¹⁴ Indexation may fuel inflation, and under circumstances, in which the level of rents increases more slowly than the level of other prices, sitting tenants will actually be worse off than new tenants. In Italy rents are indexed at only 75% percent of the consumer price index. In this way rents increase more slowly than the average consumer expenditure, and thus the sitting tenants are not likely to come into a situation in which their rents increase faster than the level of market rents.

However, in Italy this problem should not exist at all, because all tenants enjoy rents that are below market level as a consequence of the general principle of *fair rents*, and thus there is no reason to use the indexation factor to establish even lower rent for sitting tenants.

In Denmark there is only a slight element of indexation in the policy of the rent control boards by which depreciation and administration costs are adjusted yearly to compensate for increasing costs. Maintenance allowances are increased yearly by fixed amounts according to the statutes, and capital return is fixed at the original level, and has thus been frozen since cost controlled rents were introduced.¹¹⁵ However, rents have increased significantly in the same period, in particular because maintenance allocations have increased.¹¹⁶

¹¹⁴This can be the construction price index, which should reflect the cost of reconstruction the building, the consumer price index, which should reflect the expenses of tenants, or the wage price index, which should reflect the tenants' ability to pay rent.

¹¹⁵See *supra* p. 31.

¹¹⁶From 1979 to 1992 maintenance allocations have gone up from DKK 17 pr. sq. meter to DKK 56.

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There is a clear difference between the German system using comparative rents on the one side, and the Danish and Italian systems using tariffs on the other. The German system allows sitting tenants to pay market rent, though a factor of delay has been applied. In both the Danish and Italian systems no tenants pay market rent, and rent increases are subject only partly to indexation. In this way rents are lower in these countries and they stay lower through the period of contract.

Rent increases due to improvements

When a property is improved, it is essentially changed. Any change in the property means that the landlord does not provide the property originally agreed on, and security of tenure implies the tenant should not accept any modification of contract; the security of tenure is a defensive right which allows the tenant to resist changes, regardless of whether these changes can be considered as improvements and thus of benefit to the tenant. On the other hand, urban renewal would become unfeasible if all tenants needed to agree on improvements. However, essentially improvements must be seen as a breach of the security of tenure, and consequently raises some problems of protection.

The first problem is whether the landlord can make any improvements at all without the consent of the tenant, or if such changes will be considered as a breach of contract. Second, which changes can be considered as improvements, and thus acceptable, and third how can the landlord calculate a rent increase on the basis of an improvement.

In Denmark and Germany, there are some provisions which allow the landlord to improve his property and to finance the improvements through rent

increases, whereas in Italy the landlord can make improvements, but it is not possible to finance them through rent increases.¹¹⁷

The definition of improvement is relative, and what may be an improvement for some tenants is not for others.¹¹⁸ Moreover, in certain cases tenants may prefer to stay without improvements, because they would not be able to afford to stay in the property after improvements have been made. In this way improvements can lead to gentrification,¹¹⁹ and a political issue arises, namely the issue of which standard should be sought after, and what should be considered as

¹¹⁷For Denmark see boligreg. loven, kap. 4. There are no explicit provisions that allow landlords to make improvements, but as the Rent Restriction Act contains provisions which allow the landlord to raise rent if improvements have been made, it is implicit that improvements can be made. For Germany see BGB § 541b and MHG § 3. The definition of improvements in German law is slightly more narrow, however, in German law, as some services such as cable TV are not considered to be improvements. For Italy see cod.civ., art. 1582. Some work will, however, change the status of the house according to the calculation tables of the Fair Rents Act, and in turn lead to a rent increase, but only extraordinary maintenance work can be financed directly through rent increases, see legge n. 392/78, art. 23.

¹¹⁸For example, if a tenant has made some individual investments in new energy-conserving windows, and the landlord afterwards wants to renovate the windows of the entire building; if a landlord wants to renovate the backyard of the house and establish outdoor facilities for the tenants instead of a clothes-yard, a tenant may argue that the substitution of a clothes-yard with outdoor facilities is not an improvement. From Danish law, see UfR 1962, p. 548H, where the landlord wanted to install refrigerators in all apartments, and a tenant who had already bought one protested. In supreme court it was considered *not* to be an improvement, that would allow the landlord to increase the rent. See also about the concept of improvements Krag Jespersen (1989b), pp. 170-190.

¹¹⁹Gentrification is a change of neighborhood due to renovation, where tenants also change, because old tenants move out, and richer new tenants, who are able to afford higher rents, move in. The old tenants move on to other districts of low standard housing and low rents. See Anon (1988), pp. 1835-1843.

luxury.¹²⁰ This question is also closely related to the question of which rent increases are allowed.

The policy of rent increases on the basis of improvements is a balance between two objectives, security of tenure and urban renewal. Landlords will be reluctant to make any improvements if they do not get a reasonable return on their investment, so if the protection of tenants becomes too strong there will be no urban renewal. On the other hand, a very liberal system for rent increases will lead to a serious threat against the security of tenure of sitting tenants.¹²¹

In Denmark landlords are allowed a return on investment in improvements, which is based on the costs of improvement. Accordingly, the landlord can calculate a rent increase on the basis of his investment.¹²² This is the case also

¹²⁰The Ølgaard Committee made the point that by creating a uniform high standard people are deprived of the choice of a cheap place to live. See *Boligmasse og boligkvalitet* (1990), pp. 37-40.

¹²¹A special problem that rises from the calculation of rent increases is the allocation of the investment between maintenance and improvements, as most improvements also contain an element of maintenance, because some maintenance work is done at the same time. If this element is estimated as very low, landlords will tend to improve their houses rather than maintain them. On the other hand, if the element is estimated as too high, the return on investment becomes too low, and there will be no improvements made at all. In Italy landlords can demand a rent increase on the basis of the costs of major maintenance works, but not on the basis of improvements, see legge n. 392/78, art. 23.

¹²²The landlord can demand a rent increase which covers interest on the investment, depreciation, maintenance, insurance and administration of the improvements. Calculation of rent increases due to improvements are difficult to calculate. First, it must be decided how much of the actual investment has gone to improvements, and how much is maintenance, see *supra* n. 121. For example, in Copenhagen 33% of the investment in insulated glass units is considered to be maintenance of the old windows. In Århus, it is only considered to be 25%. Second, interest rates and the value of professional services rendered by the landlord himself are often matters in question.

in Germany, and the two systems seem quite similar.¹²³ Both systems allow landlords to improve their houses and to finance the improvements through rent

Tenants must be given 3 months notice of the rent increase, and if they choose to protest, the landlord must bring a case before the rent tribunal or the rent control board. In the case where the landlord plans to increase the rents on the basis of improvements, the tenant has certain right to secure them against excessive rent increases following improvements.

If a dwelling is improved and this will lead to a rent increase larger than DKK 60 per sq. meter per year (together with other improvements made during the last 3 years), the tenants must be given notice before the work starts. The tenants can test the acceptability of the improvements planned and the following rent increase at the rent control board, and if the landlord has owned the house for less than three years, a majority of the tenants can -- regardless of the acceptability -- demand that the project is postponed until the landlord has owned the house for at least five years.

In the case of rent increases larger than DKK 120 per sq. meter per year, the tenants are entitled to have a substitute property at the same standard and price level as the old one. If the landlord cannot provide a substitute property -- and it has been demanded by the tenant -- the rent increase cannot exceed DKK 120 per sq. meter per year.

The most recent change in the Danish legal system has given the landlord an opportunity to obtain an approval for a rent increase due to improvements in advance, see lovforslag nr. 205 af 16/5 1991. This change has been motivated by the complexity of the calculation system, and insecurity to which landlords were left when they wanted to make improvements. Before the rent control board could only examine the rent increases after improvements had been made, and the boards would in many cases reduce the rent increase demanded by landlords, because a part of the improvements made were considered to be a maintenance substitute; landlords were thus reluctant to improve houses, because they did not know the effect of their investment beforehand. With this recent change in the Rent Restrictions Act, they will at least know the economic consequences of a project before they begin it.

¹²³See MHG § 3. Rents in Germany can be increased by 11% of the improvement costs. If work consists of combined maintenance and improvement, the maintenance element should be deducted from the improvement, and if the work is financed by cheap public loans the rent increase must be reduced.

increases, and at the same time the systems protect tenants against very steep rent increases which may be unaffordable for them.¹²⁴

The Italian system on the other hand does not accept rent increases in the case of improvements, and in that way the security of tenure is even stronger at this point than both in Germany and in Denmark, but it is at the cost of urban renewal as landlords have no incentive to improve their houses.

However, this problem is different from the general rent increase problem, as the main issue is not the landlord's capital rights opposed to the tenant's security of tenure, but rather the security of tenure opposed to another social objective, namely the improvement of the housing stock. By restricting access to rent increases on the basis of improvements the landlord is deprived of one way of investing more money in his property.

This raises the very complex political problem of balancing security of tenure with the general objective of improvement of the housing stock, and here both Danish and German rent policy compromise security of tenure in order to allow some urban renovation, whereas in Italy such a compromise has not been made.

The problems of economic rent control

The problem of how to allow rent increases during the lease still seem to be insoluble. A completely free market does not seem possible; in Germany, where the most market-oriented regime is found, a market substitute has been set up in the shape of comparable rents. Basically the German system can be described as a free market system, where rent increases only need to be

¹²⁴See *supra* n. 122, and BGB § 541b, according to which a tenant does not need to accept improvements which cause hardship to him.

controlled and verified, and the landlord is allowed to charge the rent that he otherwise would have in a free market. However, any rent increase endangers a tenant's security of tenure, because it will become more difficult for the tenant to meet his obligations; and also in the German system, there are measures to protect sitting tenants against excessive rent increases.¹²⁵

Nevertheless, there are some distinct tendencies that can be pointed out.

In all three countries, cost increases can be passed on to the tenant.¹²⁶ Cost increases tend to follow inflation, and cost based rent increases protect the landlord from loss of income.

In both Denmark and Germany, improvements can be made, and the tenants can be charged a rent increase on the basis of the improvements. It is important to note that improvements change the entire contract, and rent increases can be so high, that security of tenure almost disappears. This must be seen as the result of a political objective to improve the housing stock, which would be impossible to finance if rent increases were not allowed.

It is the rent increases due to a demand for an increased capital return which are the core of the rent increase problem. Here the countries use different systems, and it is obviously a political solution as to whether the landlord should be allowed to increase his capital return at all, or the tenant's security of tenure

¹²⁵See *supra* p. 116.

¹²⁶From a constitutional point of view, this can be seen as a way to indemnify the landlord, so he still gets the same benefit from the contract as he used to. The argument can be found in *Blake-Madigan v. Attorney General* (*supra* Ch. 3 n. 12) and UfR 1965, p. 293H (*supra* p. 48).

is so strong that he should be able to sit for the same rent as he has always done.¹²⁷

No matter which kind of rent control is used, it can be seen that the protection of tenants' security of tenure leads to rents below market level and to other restraints on a landlord's ability to enjoy the full economic use of his property. These restraints on the landlord correspond with benefits for the tenant; in other words by letting out a property under rent control the landlord must give up some of his property rights which are transferred to the tenant.

This is, however, a quite trivial point; it does not differ from any other contract, as the concept of a contract is precisely exchange of rights. What makes rent control special in this context is that some of the rights are transferred to the tenant without any consideration, and these rights grow over time. Tenants that have been sitting for a period of time enjoy lower rents and better protection against eviction than new tenants. At the same time old tenants -- like all tenants -- give up their accumulated rights when they move, and without any compensation, because they are not considered to have any economic value in the first place.¹²⁸

Consequently, sitting tenants who enjoy these rights are not likely to give them up, as they are not compensated. Tensions between landlords and tenants become stronger, because landlords have absolutely no incentive to keep their tenants; on the contrary, when a tenant moves out, there is an opportunity for

¹²⁷It can also be argued that the tenant has a right to take part in the capital gains on the property that he is occupying, because the value added to the property is created by society rather than by the landlord, see Brennan (1988), pp. 76-79, and Radin (1988), pp. 80-83.

¹²⁸If the security of tenure is considered to have an economic value this will imply a transfer from the landlord to the tenant in the first place. This can be argued to constitute a taking, which would be constitutionally illegitimate. See UfR 1990 p. 36H (*supra* p. 50).

the landlord to cash in on the tenant's right -- either by increasing the rent for the new tenant, or with alternative allocation procedures.¹²⁹

Thus security of tenure must be acknowledged as an economic right.

Only in Denmark tenants do have a way to capitalize their rights, and even in this case it is only when they want to exchange property that it is possible.¹³⁰

¹²⁹The problem cannot be overcome simply by introducing full-scale rent control without vacancy decontrol, because the allocation right will still have some value, though it may become more difficult for the landlord to find economic use for it.

It could be argued that not the rent control, but rather the vacancy decontrol leads to a situation in which landlords and tenants are opposed to each other. If the rent control also covers new tenants, the landlord has no incentive to terminate old leases, as tenants under a new lease will benefit from the same low rent. For the landlord there will make no difference whether one or another tenant pays a rent controlled rent, as long as the landlord does not have any personal need for the allocation right. It can be argued that in this way the allocation right and security of tenure really do not have any economic value for the landlord, and the pressure is taken off sitting tenants. This is, however, a fiction, as security of tenure still has economic value for the sitting tenant, because the tenant, as a consequence of the shortage following rent control, will have difficulties finding alternative housing at the same rent. Consequently, if the tenant gives up his lease under full-scale rent control, it may be more difficult for the landlord to make economic use of the allocation right, but for the tenant the problem remains the same, because he will not easily be able to enter a new contract. Thus, neither of the parties can benefit from the tenant giving up his security of tenure, and in this way the complete fiction has been created; the mere prevention of somebody making use of a right, does not necessarily mean that the right does not exist.

This is very close to the situation in Denmark where the fiction is almost complete. However, in Denmark the right to exchange has been introduced to allow tenants to exchange their property and thus make economic use of their security of tenure. In this way tenants have actually taken over a part of the landlords' allocation right, and as pointed out earlier this is questionable from a constitutional point of view, see *supra* p. 50. Moreover, full-scale rent control causes other problems which have been pointed out, see *supra* p. 103.

¹³⁰However, the Danish right to exchange property does not include the right to sell the right to the property. It is assumed at on the one hand that tenure has no value, and on the other hand that the exchange right was introduced to increase mobility in the housing market, because

None of the countries allows tenants to obtain cash from their security of tenure, though it may be one way to overcome the problem.¹³¹

There are, however, difficulties in finding a way to allow tenants to transfer their rights.¹³² If all tenants were allowed to cash in on their right to security of tenure, either by selling to any third party or back to the landlord, the entire market for private tenancies would be based on a key money concept where tenants pay other tenants to obtain a property, and in the end the entire private rental market would take the form of the market for private ownership, where property is bought rather than rented. One of the main reasons for people to enter the private rental market is that they cannot afford to buy their own property, and this solution would prevent many people from entering the housing market at all.

tenants could not find other property with the same low rent. In this way some property is actually passed on for an indefinite period of time, as it is too valuable for the tenants to abandon. See also *supra* p. 88.

¹³¹A tenant may live in a house for a long time and by paying the rent, he may not gain title to the property, but he is definitely contributing to the increase in capital. In this context it is also notable that the location factor as one of the most important factors in the pricing of real estate is very much influenced by the type of neighborhood and thus the neighbors. Consequently, tenants collectively contribute to the determination of the location factor. See also Brennan (1988), pp. 76-79.

¹³²One author suggests -- as a path to deregulation -- that a tenant should be able to sell his security of tenure back to the landlord after negotiation. It is assumed that afterwards the landlord can rent the property at the free market rent. This solution may be useful for the purpose of deregulation. However, as pointed out deregulation does not solve the problem of security of tenure, see *supra* p. 17. There is a general problem in this solution too, as negotiations between landlord and tenant will be impossible to conduct; in a position where the tenant needs to move, the landlord is obviously interested in paying as little as possible. There is, however, a sound element in the argument; when the tenant moves out, the landlord regains the full economic use of the property, which has been restricted by the sitting tenants. This is worth paying for, and the landlord should pay for it. See Wolkoff (1990), pp. 261-263.

Moreover, such a concept based on key money would permanently lower the landlords' return and there would still remain a maintenance problem.¹³³

Enforcement

Enforcement is a very important issue in rent control law. A regulatory system, such as rent control can be made with the best intentions, but it will not work unless it is enforced. Tenants are often both ignorant of their rights and held in a position where they do not want to cause trouble, because they are afraid of the consequences. Tenants may also fear entering into litigation, which is a long, costly and sometimes unpredictable process.¹³⁴

One of the most important issues in the enforcement of rent control is how to create a comprehensive system in which the parties understand the system and know their rights. One way to make the system accessible -- if not understandable -- to the parties is the use of model contracts.¹³⁵

Another way to ensure that the tenant knows his rights is to condition the validity of legally binding notices on a certain content. The form of notices can

¹³³If the landlord could increase rents freely when a property was transferred, there would be no point in taking key money from a new tenant. Accordingly, the right to sit should be transferable and rents permanently lowered. This would in turn create a maintenance problem -- apart from also being questionable from a constitutional point of view.

¹³⁴There is also a sociological problem of landlord-tenant relationship, especially where the landlord and tenant live in the same house, which is often the case particularly in Germany and Italy. In this situation any dispute between the parties may have a strong impact on the life of the parties. Accordingly, the parties will be even more reluctant to insist on their rights. In Germany and Denmark tenancies regarding two-family houses can be terminated on discretionary grounds when the landlord himself lives in the house. See *supra* n. 58.

¹³⁵In Denmark many clauses are written into the model contract only for the purpose of explanation as they would apply anyway, because they are copied from the Rent Act, where they have been made invariable. Thus the only reason to repeat such clauses in a model contract is to ensure that the parties have easy access to them. See also *supra* p. 78.

be seen as a way to achieve a higher level of information to tenants, and it gives the tenant who is put in a difficult position an immediate possibility of questioning the legality of the landlord's claim.¹³⁶

Two other problems of enforcement are access to litigation, and the escape strategies of landlords. Access to litigation is a problem which involves the conflict between landlord and tenant at the individual level, where they have opposed rights. Escape strategies are more abstract approaches to enforcement, because landlords who try to escape rent control are often not in conflict with individual tenants, but they undermine the policy of rent control.¹³⁷

Maintenance can be mentioned as the last enforcement problem. Landlords can lower the maintenance standard, and thus also the value of the rental property. It can be seen as means by which the market value moves closer to

¹³⁶In both Denmark and Germany a notice of termination must contain certain information about the reason for termination, and the landlord must also inform the tenant about his right to set up an objection, otherwise the notice will be void, (see *lejeloven* § 87 and *BGB* § 564a). In the case of rent increases some information about how the rent increase is calculated, (see *boligreg.loven* §§ 12-13, *MHG* § 2). According to these provisions, notice must be given for any rent increase through a special procedure, otherwise it will be void. In Denmark this procedure includes three months notice, the budget and the maintenance accounts must follow the notice, and the tenants must be informed about their right to object. In Germany the comparable property must be described. See also *BVerfGE* 37 p. 132 (*supra* p. 54). Moreover, tenants must agree to the rent increase. In both countries it is the landlord who must take legal action in the case of a dispute, see *boligreg.loven* § 13 and *MHG* § 2 (3). In Italy there are no provisions concerning the procedure for rent increases.

¹³⁷Escape strategies are ways to avoid the house being subject to rent control, e.g., when a landlord leaves his house empty no tenant is offended, but the housing stock has been diminished, and it becomes more difficult for tenants to find a new place to live. If a landlord and a tenant agree on key money, the tenant may not perceive this as an offense, because his only alternative would be not to obtain a controlled property, but the policy objectives of rent control have been infringed.

the actual rent, and if there is no obligation for the landlord to maintain his house, the long term effect of rent control will be a deterioration of the housing stock.¹³⁸

Court systems

Easy, cheap and quick access to litigation is necessary to ensure the enforcement of rent control. If litigation is not accessible or simply too slow or costly, tenants will be reluctant to question the claims of the landlord.¹³⁹

Easy, but not necessarily cheap access to the court is achieved in Denmark and Germany by a system of reversed initiative, in which the landlord has to bring the case to court if the tenant objects.¹⁴⁰ In this way the landlord must sue the tenant in order to justify his claim. Another way to ease access to the court is through invariable clauses regarding the venue. In all three countries the venue for rent control cases is in the area of the property, and thus the tenant will not have to go far to go to court.¹⁴¹

Cheap access to litigation is partly achieved by the application of an inquisitorial procedure in rent control cases. When this procedure is applied, the judge can ask the parties to provide information and if necessary seek information elsewhere, in order to achieve a correct decision in substance. Some elements

¹³⁸See *supra* p. 10.

¹³⁹Litigation can be made expensive and slow in order to force the parties to seek arbitration or a settlement out of court instead of litigation. However in rent law, the parties are not likely to settle out of court; the parties are uneven, and bargaining has become impossible because and the need for security of tenure has taken away the bargaining instruments on both sides, i.e., the right to opt out of the contract.

¹⁴⁰See *supra* n. 136.

¹⁴¹See *lejeloven* § 107, *Zivilprozeßordnung* §§ 29a and 1025a and *legge* n. 392/78, art. 45 and 54.

of this system can be found in all three countries, and in this way the parties do not necessarily need legal advice in court.¹⁴²

Cheap and quick litigation can also be obtained through the use of rent control boards. Such boards are found in Denmark, but not in Germany or Italy.¹⁴³

¹⁴²In Denmark the system applies to rent control boards, but not rent tribunals, see *infra* n. 143; in Germany courts have some inquisitorial powers in rent control cases, *Zivilprozeßordnung*, art. 308a, though the general principle of court procedures is not inquisitorial; in Italy courts have general inquisitorial powers in rent control cases, see legge n. 392/78, art. 47.

¹⁴³In Denmark there are both rent tribunals, which are courts and rent control boards. Such boards are also known in Ireland, the UK, and the USA.

All disputes under the Rent Act are brought before the Rent Tribunal, which is the local court in the district of the dwelling. In most situations the judicial judge will be assisted by two *lay* judges. These *lay* judges are by no means *lay*, as they represent the landlords and the tenants' organizations. Normally they are lawyers, administrators, landlords or tenant representatives. Consequently, they are very knowledgeable in their field, and this has even been made a condition for appointment.

Disputes under the Rent Restrictions Act are brought for the rent control board, which is a body within the municipal administration, set up according to the Rent Restrictions Act. It has three members -- as the Rent Tribunal, one representative of landlords, one of tenants and one neutral member with a university diploma in law. The rent control board is independent in the sense that no other administrative body can instruct the board about how to decide in cases. Moreover, as the board is decides in disputes between private parties, there are many similarities to a tribunal, though rent control boards are not considered to be a judicial court in the classical constitutional sense.

The difference between tribunals and rent control boards is, however, significant. The board is much more accessible than the tribunal. Only in 1991 a general but modest fee was introduced (DKK 100 pr. rental unit), before which the services of the board were free to everybody. A request does not need any particular form to be proceeded with; a tenant can start a case simply by writing a postcard stating: "I believe that my rent is too high." The procedure is also different from normal court procedure, as the board applies an inquisitorial procedure which is almost exclusively carried out in writing, and thus the parties do not need to be presented by lawyers. The board normally work faster than the Court, which also aids accessibility.

Legal aid is also used to lower litigation costs for tenants, and thus to enforce rent control.¹⁴⁴

In all three countries, some measure has been taken to ensure accessibility to courts in the case of rent control disputes. However, it is worthwhile noting that even though such measures have been taken, there are many differences between court practices in the three countries, and in Italy in particular court cases can take very long time -- sometimes even years -- whereas Danish rent control boards normally reach a decision within a few months.

Escape strategies

When rent control is introduced, it restrains the profitability of property, as rents cannot go above the ceiling imposed by rent control. However, rent control itself does not control alternative ways of using the property, and thus induce landlords to develop escape strategies, where houses are used in an alternative way in order to achieve an economic rent.

These escape strategies differ from situations in which the landlord tries to adapt to rent control by screening, lowering the maintenance standard, etc. When a landlord escapes, he simply opts out of the private rental market and uses his property for alternative purposes. Such escape strategies lead to a need for enforcement on a more general level, because otherwise rent control will eventually lead to the end of the private rental market.

There are several means of escape. The landlord can simply let his property stay empty. He can choose to demolish a property in order to find alternative use for the land. He can use the property for purposes other than private rental

¹⁴⁴Legal aid is available in Denmark and Germany for people with low incomes. See lovbekendtgørelse nr. 748 af 1/12 1989 om rettens pleje §§ 330-336c and Zivilproceßordnung § 114.

housing, for example, office space, non-regulated short term housing, or he can convert the house into condominiums which can be sold at market prices.¹⁴⁵

If rent control is strong and these means of escape are open to landlords, the incentive to keep the property as a private rented property obviously becomes very slight.

In Denmark there is a very strong legal framework which protects the housing stock from such escapes. Condominium conversion, demolition and abolition of dwellings are not permitted in general. On the other hand, conversion into multi-ownership housing is strongly encouraged for political reasons, and in this way the private rental sector is declining, though property remains in use for residential housing.¹⁴⁶

¹⁴⁵See Stanbury and Todd (1990), pp. 403-406.

¹⁴⁶In Denmark there has been a distinct move from the private rented sector to private home ownership through new construction during the last 50 years, as rent control has made it unattractive for private entrepreneurs to construct private rented housing.

During the same period the rental housing stock has also been eroded. Condominium conversion was one of the most popular ways to escape rent control during the seventies, as condominiums were sold at market price. However, in Denmark the possibility of conversion was only open for a very short period of time. Afterwards, strict general restrictions were introduced which make it virtually impossible to convert the existing housing stock into condominiums. Only houses constructed after 1966 or buildings listed as to be preserved can now be converted freely. See lovbekendtgørelse nr. 601 af 21/8 1990 om ejerlejligheder § 10.

Dwellings cannot be abolished without the consent of the local authorities, and nor can they be converted to other uses, e.g., to commercial use, See boligreg. loven § 46. Moreover, landlords are obliged to let out vacant dwellings. If a dwelling remains vacant for more than 6 weeks, the landlord is obliged to notify the local authorities, who in this case will be entitled to allocate the property to homeless, see boligreg. loven § 48. As the national register of persons is run by local authorities, they automatically register changes and make inquiries whenever nobody is registered as living in a dwelling, and accordingly enforcement is efficient.

In Germany condominium conversion is permitted, but dwellings may not be left empty for a long time or changed into commercial use.¹⁴⁷ In this way property remains in use for residential housing, even though landlords can opt out of the private rental market. However, escape from rent control is not as attractive in Germany as in Denmark, because rents are relatively high.

In Italy, however, there are only local provisions, which prohibit commercial use of residential property. In general property can be used for holiday housing, changed into condominiums, rented as office space or under non-regulated contracts, and landlords are reluctant to make any new contracts at all under rent control.¹⁴⁸

Accordingly, it can be seen that, where Denmark and Germany have a protective framework which helps to keep the housing stock intact, Italy -- which has a very rigid rent control regime -- does not have such a framework, and the result is a very clear tendency towards a decline in the Italian private rental sector.

As a consequence most old private rental property remains in use for its original purpose. However, many buildings are channeled into the multi-ownership scheme, because houses must be offered to tenants upon sale, see *lejeloven* § 100 and, see also *supra* Ch. 2 n. 10.

¹⁴⁷See *Verbot der Zweckentfremdung von Wohnraum*, Gesetz vom 4. November 1971.

¹⁴⁸See van Hees (1991), p. 24 and Venegoni (1985), pp. 284-285. Italian landlords, who often are private persons with relatively small units, often prefer to let their property stay empty instead of renting it under rent control. Security of tenure in particular causes very big problems for the group of small landlords; as property is often held for reasons other than sound investment, (house prices compared with rents really do not make any sense in Italy), these landlords simply do not accept security of tenure.

Maintenance and deterioration

Maintenance has been pointed out as one of the main problems of rent control.¹⁴⁹ The problem occurs when the landlord responds to rent control by lowering the maintenance standard. In this way rents obviously do not increase, but the rental value of property becomes lower, and thus it gets closer to the controlled rent.

It is possible for a landlord to reduce the maintenance standard because there is no direct link between the maintenance standard and the rents; and consequently, a lack of maintenance does not reduce the landlord's earnings.¹⁵⁰

Obviously, the tenant needs some protection against such a reduction in standard. Essentially, a reduction in standard can be seen as a breach of contract, because the landlord provides a property of less value than that agreed on, and the landlord is obliged to provide the property continuously and at a standard according to the contract.¹⁵¹

There are, however, two main problems which arise in this context. First, to decide which standard the parties have agreed on; second, to find out which means the tenants have to enforce it.

As a starting point the parties can agree on any standard they want -- even the very lowest. This can be seen as an expression of their freedom of contract,

¹⁴⁹See *supra* p. 10.

¹⁵⁰The landlord's earnings will only be affected when the standard becomes so low that the tenants actually find that even the controlled rent is not worth paying, i.e., when the standard becomes so low that the market value of the property falls below the controlled rent.

¹⁵¹In all three countries, it is an obligation of the landlord to maintain the house, see Lejeloven § 19; BGB § 536; cod.civ., art. 1576. See also *supra* 81.

and in a community with vacancy decontrol this causes very few problems, because the rent will correspond to the standard at the time when the contract is entered into.¹⁵²

In communities without vacancy decontrol, the rent control must be linked to a certain maintenance standard in order to avoid circumvention. This can be done in two ways: a certain standard can be assumed, or the controlled rent can be influenced by the maintenance standard.

In Denmark it is assumed that tenants at controlled rents are entitled to a certain standard of maintenance, and there is a general assumption about what the standard *should be*, and even though the parties have a freedom of contract, they normally do not agree on a lower standard, because such an agreement would imply a lower rent.¹⁵³

In Italy the age and maintenance standard are elements in the controlled rent, and accordingly tenants in poorly maintained property get a discount on the rent.¹⁵⁴

If the property does not meet the standard which the parties have agreed on, the property is considered to have a defect.¹⁵⁵ In all three countries, tenants

¹⁵²However, some minimum standards may be set by public health authorities. Such standards are set not for reasons of rent control but as minimum health guarantees. In all three countries, there are provisions concerning the obligations of the parties in the case of unhealthy living conditions in the property, see *lejeloven* § 16 stk. 2; BGB § 544; *cod.civ.*, art. 1580. See also *supra* p. 81.

¹⁵³A lower rent would apply according to the principle of equality among tenants, see *supra* p. 31 and Karnov (1989), p. 2140

¹⁵⁴See *legge n. 392/78*, art. 20 and 21.

¹⁵⁵Accordingly, defects are relative to the standard defined by the contract, and thus it can be stated, that the maintenance standard is essential to the description of the landlord's main obligation. See *Boligmasse og boligkvalitet* (1990), pp. 38-39 and also *supra* p. 81.

have certain rights in the case of defects. Most of these rights correspond to general principles from the law of obligation, according to which tenants can claim that the landlord performs according to the contract.¹⁵⁶

In case of defects that occur during the period of contract, the tenant can also claim that the landlord performs, and the real problem is rather to enforce the maintenance obligation of the landlord than to decide the extent of the obligation. Litigation over maintenance may be very costly, and it still only leaves the tenant with an economic claim against the landlord, which does not necessarily raise the property to a better state. Moreover, there is a special problem if the landlord cannot afford the necessary maintenance work.

One way to solve small maintenance problems is to allow tenants to do the repair work needed and afterwards set off the expenses against the rent. In Denmark and Germany tenants can do so.¹⁵⁷ This is a practical solution in the case of minor repair work, though major work is not likely to be undertaken in this way, because it is too costly for the tenants to afford. In Italy such right only applies to tenants in the case of urgent repairs.¹⁵⁸

¹⁵⁶The tenants can demand that the landlord brings the property up to the standard which the parties have agreed upon. The tenant is entitled to a reduction in rent and compensation for damages during the period of defect. See *lejeloven* § 11, BGB §§ 537-538 and *cod.civ.*, art. 1578. In certain situations there is a need for immediate action, and the landlord has a duty which goes beyond the duty of maintenance, and the landlord may be liable according to a theory of implied warranty of habitability, see Corodemus (1985), pp. 35-36. However, it is arguable whether tenants under rent control can claim damages in the case of defects, because damages imply an economic loss, and tenants have not incurred such a loss relative to the market rent.

¹⁵⁷See *lejeloven* § 11 and BGB § 538 (2).

¹⁵⁸See *cod.civ.*, art. 1577.

In Denmark disputes about the landlord's obligation to maintain the property can be brought before the rent control boards, and the boards can order certain work to be done.¹⁵⁹ These decisions can be made regardless of the balance of the maintenance accounts.¹⁶⁰ However, the system cannot prevent the housing stock completely from deteriorating.¹⁶¹ In Germany and Italy there are not similar means to ensure the enforcement of maintenance obligations.

Consequently, some maintenance structures can be seen in all three countries, as the landlord is obliged to maintain his house, but only in Denmark is there a very easily accessible system which allows tenants to enforce the landlord's maintenance obligation.

¹⁵⁹See boligreg. loven §§ 21-22. If the landlord does not fulfill his maintenance obligation within the stipulated time set by the rent control board, the work will be undertaken by Grundejernes Investeringsfond, a semi public administration body, which will do the required work at the expense of the landlord, and have the costs secured with a first mortgage on the house. Accordingly, even the mortgagees have to respect the tenants claim for maintenance.

¹⁶⁰Maintenance costs are calculated by law on the basis of size of the property (in sq. meters) and included in the cost controlled rents. See *supra* n. 102. Only some of the appropriation, (DKK 15 per sq. meter per year), must be paid into a special account in Grundejernes Investeringsfond, which is a semiofficial body. The rest is kept by the landlord as virtual accounts, and he has no obligation to keep these accounts separate from his personal funds. Once a year the tenants and Grundejernes Investeringsfond must be informed about the balance, appropriations and expenditure, and if the landlord fails to keep an account, the rent control board will assume that the balance of the account is equivalent to the last five years appropriations without any deduction for expenditure.

However, whether accounts are negative or positive has very little influence on the state of the house, as the landlord is obliged to maintain the house, no matter what the balance of the account. Only the individual account may have some importance for the maintenance obligation. The tenants can always complain to the rent control board about the standard of maintenance, and the board can order the landlord to do certain work regardless of the status of the maintenance accounts. See also *supra* p. 81.

¹⁶¹See Boligmasse og boligkvalitet (1988), pp. 44-46.

Approaches to enforcement

Enforcement structures are important to make rent control work, and there seem to be substantial differences between the approaches to enforcement in the different countries. Enforcement must, however, be seen in the context of substantial rent control.

Denmark has a very strong enforcement system in which rent control boards play a major role in easy access to litigation, and where escape from rent control has become very difficult -- if not impossible. This strong enforcement system corresponds to a very strong rent control in substance.

On the other hand Germany and Italy do not have strong enforcement systems. As for Germany, this may correspond very well with the substance of rent control, whereas for Italy, the gap between strong substantial rent control and in particular the many possibilities for escape, seem to cause problems for the provision of rental housing in Italy, and accordingly the Italian rent control policy seems to be less coherent than the policy of Denmark and Germany.

Structural overview

It is a political choice how far rent control should be taken in order to ensure security of tenure. Some of the contractual regulation may serve as consumer protection, rather than as specific issues of security of tenure. However, such provisions can also be seen as issues of rent control, which have a value which is not only social but also economic.

The economic structures show that all three countries apply some kind of cost controlled rent, by which certain costs can be transferred to tenants. The main question of economic structures is, however, how to calculate the non-cost element of the rent, which covers administration, maintenance and capital return.

Basically there are two ways to approach the non-cost element; through market simulation or through tariffs.

In Germany a policy of market simulation is followed, and this can be seen as a way to try to avoid the problems of rent control. However, there is still an element of price control, because rents cannot be increased by more than 20% over a three-year period.

In Denmark and Italy tariffs are used. These tariffs are set arbitrarily, though the Italian concept of tariffs can be seen as an attempt to simulate the long term equilibrium in the housing market, and thus to provide *fair rents* from a market oriented point of view.

How tariffs are set is unimportant as long as the use of tariffs leads to rents below market level, because they will lead to a situation where security of tenure has an economic value, and it is not feasible to let the tenants cash in on this economic value.

In Germany rent control does not apply to new contracts, and there is no need for control of such contracts, because there is no security of tenure to protect. Only if the objectives of the rent control policy are extended to cover affordability does control of new contracts become meaningful.

There are weak spots in the structures which also must be pointed out. First, the lack of security of tenure in Italy, where tenants can be evicted every 4 years. Second, the possibility to escape rent control -- especially in Italy makes rent control work less efficiently. Third, the right to improve property and demand rent increases to cover the costs of improvement. Fourth, the right of Danish tenants to buy their property and convert it into a property under the multi-ownership scheme.

The first two are real weak spots which endanger security of tenure and the success of rent control policy, whereas the last two are inroads into security of tenure chosen for objectives other than those of rent control policy.

When the three systems are compared, the German system leaves an impression of being a coherent system, which protects the tenant's security of tenure effectively and at the same time tries to minimize the economic distortion which is an effect of rent control. However, there are restrictions to the right of the tenant to change to use of the property, and security of tenure is endangered by the landlord's right to terminate on the grounds of economic use.

On the other hand, Danish law fulfills the objective of security of tenure extremely effectively; both contractual and economic protection of tenants is very strong, and the enforcement is efficient. However, rents are controlled at a level below the market level, and the framework of rent control has imposed many restrictions on landlords' use of property; they have in part lost their right to allocate property, they cannot change the use of the property, make substantial improvements or opt out of the market by letting the property remain empty.

In Italy security of tenure is not very effectively guaranteed, and at the same time the system is not very coherent. It leaves landlords and tenants in a position of uncertainty, with a system of very strong rent control which can very easily be circumvented. It is a system in which tenants may benefit from low rents, but without knowing how long they be able to do so.

In the political choice between rent control regimes, the German regime can be said to be a minimum solution, which gives tenants the minimum security of tenure which is required in a welfare state. The Danish regime can be said to

be a maximum solution, where rent control is taken as far as possible, and the Italian regime can be said to be no solution at all.



CHAPTER 5

CONCLUSIONS

Free rents and security of tenure are incompatible with each other. When tenants are granted security of tenure, a distortion of rents occurs at some time. This distortion is a product of rent control, which is a part of security of tenure, and it becomes more difficult for tenants to move, because they will not be able to find another property at the same price elsewhere. In turn, this makes it important to acknowledge tenants' security of tenure as an economic right.

This right has a value in a market with increasing prices where controlled rents are lagging behind, as the value of the right can be seen as the discount which tenants obtain due to rent control. Even in the German system, where rents should follow the market, security of tenure becomes of value in this way, as German tenants are protected from rent increases exceeding 20% in a three year period.

It has been pointed out, that there is a trend towards more security of tenure. However, it would be wrong to perceive security of tenure as a fundamental right, a personal freedom that cannot be taken away. Security of tenure is very much an economic right; the right to use your home in the way you want, for as long as you want, and to take part in profits owing to fluctuations in the market. It is a right which is obtained at the expense of the landlord, and it can be seen as a way to bring about equality between home-owners and tenants. This may be seen as a social trend, but not as a fundamental right.

At the same time tenants are perceived as a group opposed to home-owners. They do not buy their property, and when they move out, they give up their security of tenure -- or more correctly, it is transferred back to the landlord, who can either make economic use of it by renting at higher rent, or, under complete rent control, use one of the alternative allocation methods. Accordingly, security of tenure is not perceived as an economic right, and it is not protected as such. What is really wrong with rent control is that rights in this way are acknowledged as extremely important, and at the same time they are not accepted as having any value.

It has been pointed out that a straightforward solution to this problem is not feasible, because it would simply be another way of changing the entire housing market into private home-ownership. If the right to security of tenure can be capitalized, there will be only a slight difference between the right to sit and the right to own.

In the case of vacancy decontrol, it is possible for the parties to calculate the value of security of tenure in the rent, and presumably tenants should be interested in paying for additional security of tenure.¹

The tensions arise during the period of contract. The landlord will over time see market rents rise beyond the actual rent, and he will be interested in making inroads into the security of tenure, either by raising the rent or by evicting the tenant, and finding a new one who will pay a higher rent. On the other hand, the tenant will stay even longer than needed in order to benefit from the low rent. Here the distortion becomes clear, and this is the situation in which the tenant needs an adequate bargaining tool.

¹This is the case in the new British regime, see *supra* Ch. 2 n. 3. However, it remains to be seen whether the system will function according to the intentions.

A bargaining power approach

The weakness of tenants and the need for acknowledgment of the economic value of security of tenure, can also be seen from another side as a lack of bargaining power. In many cases landlords are professionals and tenants are consumers. However, the most important issue in the balance between the parties is that tenants have not only an economic interest in their property. Tenants live in their property, and sitting tenants in particular are in a very weak bargaining situation because they have no way to threaten the landlord. They cannot opt out of the contract; in that situation they give up their security of tenure, and this would in no way be a threat to the landlord.

Even if the parties were not uneven from the beginning, they become uneven during the period of contract, because the tenant obtains economic benefits from security of tenure, and -- due to his dependence on security of tenure -- he becomes dependent on the landlord.

High transaction costs imposed on the landlord would be a way to weaken the landlord's position. Such costs would make it more attractive to keep tenants for a longer period, and consequently the landlord would be less interesting in maximizing the rent of the tenants, taking them to the limit of their ability. Transaction costs can be document tax, real estate agent fees, etc., and obviously there should not be any way to agree that tenants should carry these costs. Another way of increasing transaction costs is to limit the landlord's claim for maintenance, when a tenant moves out; in this way the landlord will be forced to pay more renovation costs when the tenant is changed. Also a general right for tenants to be compensated for moving costs in the case where the landlord terminates on the grounds of own use can be seen as a way to

enhance the bargaining power of tenants.² The landlord might not be so keen on evicting tenants, if eviction is connected with payment of compensation.

Such costs will indirectly make it more difficult for the landlord to increase rents, if the threat of losing a tenant becomes substantial. However, tenants sitting for a long period will be no better protected than those sitting for a short period of time. On the contrary, tenants sitting for a long period will often have a relatively larger discount on the rent, and thus the incentive for the landlord to change tenants will also be greater.

A solution to this problem could also be found in higher deposits. In all three countries deposits are controlled. In this way deposits play a relatively insignificant role in the economics of rental housing.

If deposits were paid not only when a contract were entered into, but every month during the period of contract, tenants would over time build up considerable deposits. These deposits would change the balance in the relationship between landlord and tenant, as landlords with tenants staying for a long period, would benefit from large deposits. Moreover, when tenants moved out after a long period, the landlord would have to repay a substantial deposit. In turn, this would give sitting tenants bargaining power in relation to the landlord, as the economy of the property is connected to the length of the tenures.³

²This is the case in the Netherlands, see *supra* Ch. 2 n. 3.

³It can be argued that such deposits would merely add to the burden of rent that tenants have to pay. This would be correct if rents were calculated according to the investment in housing. As the deposit -- sooner or later -- must be paid back, only the interest from it could be calculated as an income. However, if the rent is set according to what prospective tenants are able to pay, a payment deposit effectively reduces the tenant's ability to pay rent, and for the tenant who intends to stay for a period of time, it makes no difference in the first place whether it is rent or deposits that is paid. Consequently such deposits would only reduce the rent burden on tenants. See *supra* n. 21.

From a broader economic point of view, such a regime can be seen as compulsory saving, where all tenants save money just as homeowners, thus making it easier for them to move because they move out with a cash cushion. At the same time landlords are provided with cheap liquidity from deposits and are made dependent on their tenants. The price to be paid for this solution will obviously be higher rents in general, as the rents will include these deposits and thus contain a savings element.

Final Remarks

The issue of security of tenure may be an issue of social rights, but eventually it leads to rent control, at which point it becomes an economic issue. It seems that the entire problem of security of tenure becomes less complicated when it is accepted that tenants rights also have some economic value. Somebody has to pay in the end; if the tenants do not pay, and the authorities do not pay for the tenants, the landlords must pay. However, this conclusion also leads back to the issue of affordability. Affordability has been discarded as an objective of rent control in this paper, but still in both Denmark and Italy rents are controlled at a level lower than the market level, and this cannot be justified by the need for security of tenure.

Affordability is an important issue, and obviously rent control and social policy are interdependent; but it is another study that needs to be carried out to find out how much people are actually willing to spend on housing, and when housing becomes *unacceptably expensive* from a social point of view.

Moreover, in Germany deposits are paid into separate accounts and the landlord must pay interest to the tenant from these deposits. This system would not work very well with large deposits; if deposits are to be an incentive for the landlord to continue the lease, he must also have some benefit from the deposits. The Danish system, where deposits are secured with a first mortgage in the house, would give sufficient security for the tenants.

Constitutionality is another important issue, which has been touched upon. Security of tenure seems to meet some constitutional obstacles, in particular when it is confronted with the property rights of landlords. These obstacles vary from country to country, but it is worth noting that in all three countries rent control has become a constitutional issue, and it seems that rent control on the one side is balanced against property rights, and on the other social rights are not given substance in constitutional court cases. In this way rent control law seems to be taken close to its constitutional limits. It is a political matter as to what these limits are, but it remains to be answered why rent control has become such a strong political issue.

The objective of this paper was to find out how much or how little legislation was needed to give tenants security of tenure. This question is not easily answered, because security of tenure can be more or less intense, and there will be different answers depending on what intensity of security of tenure is required.

The German system can be pointed out as a minimum system, which offers security of tenure with few economic guarantees. Obviously, this system creates less distortion than the other systems, because the intensity of control is lower.

The Danish system can be pointed out as a maximum system, which offers almost complete security of tenure, which includes many economic guarantees. This system suffers from all the repercussions of rent control.

The Italian system offers no solution at all. It controls rents, allows escapes, provides complete security of tenure which is discontinued every fourth year, when tenants can be evicted freely. The lack of coherence is substantial, and from the Italian experience it can be concluded that adequate enforcement structures are essential to rent control.

There is no ideal solution to rent control as the autonomy of parties and free market on the one side and invariable law and social objectives on the other are incompatible. However, the German system is the only one that provides vacancy decontrol which is very important, because it provides a solution to some of the problems of rent control without endangering the security of tenure. In this way German law seems to separate the objectives of affordability and security of tenure, and concentrate on security of tenure. Consequently, it is closest to the objective of this paper.

However, when security of tenure is considered to be an economic right, it becomes *only* a matter of money: Who is going to pay for housing services, and who is going to take part in the capital gains on real estate? These are questions of redistribution, and they are not questions for a lawyer to answer.

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